

# INCOME TAX

AND

## PROFITS TAX

BY

ERNEST EVAN SPICER, F.C.A.

AND THE LATE

ERNEST C. PEGLER, F.C.A.

**EIGHTEENTH EDITION**

BY

H. A. R. J. WILSON, F.C.A., F.S.A.A.



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# PREFACE TO THE EIGHTEENTH EDITION

The spate of new and involved legislation within the past few years has made it necessary for me to continue to be somewhat selective in the new matter discussed in detail, in order to maintain my aim of setting out the law and practice as clearly and as simply as possible. Some of the less essential points of detail have not, therefore, been exemplified.

It will be found, however, that this edition, like its predecessors, contains a comprehensive exposition of the subject. All legislation up to the end of 1947, and all important judicial decisions have been dealt with.

The acute shortage of paper and congestion in the printing and binding industries continue to occasion delay, which is greatly to be regretted, but these are circumstances beyond my control. A supplement containing the provisions of the Finance Act, 1948, will follow as soon as this Act has been passed.

The appendices continue to be a valuable part of the book, and references in the text to the Acts and Reports facilitate reference where necessary.

My grateful acknowledgments are due to Mr. A. E. LANGTON, LL.B.(Lond.), F.C.A., F.S.A.A., for his great help in producing this edition, and I thank also the many readers who have been good enough to send me suggestions, which I hope they will continue to do.

H. A. R. J. WILSON.

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**WILSON AND HEATON ON THE INCOME TAX**

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## ABBREVIATIONS USED IN REFERENCE TO CASES CITED

ABBREVIATION.	REPORTS.
A.E.R. . . . .	All England Reports.
A.C. . . . .	} Law Reports, Appeal Cases.
App. Cas. . . . .	
A.T.C. . . . .	Annotated Tax Cases.
C.D. . . . .	} Law Reports, Chancery Division.
Ch. . . . .	
Curt. . . . .	Curteis' Ecclesiastical Reports, 1834-44.
Ex. D. . . . .	Law Reports, Exchequer Division.
F. . . . .	Fraser (Court of Session Cases, 5th Series).
J. & H. . . . .	Johnson's and Hemmings Vice-Chancellor's Reports, 1859-62.
J.P. . . . .	Justice of the Peace.
K.B. . . . .	Law Reports, King's Bench Division.
L.J.K.B. . . . .	Law Journal Reports, King's Bench Division.
L.R., E. and I. App.	Law Reports, English and Irish Appeal Cases— House of Lords.
L.T. . . . .	Law Times Reports.
Q.B. . . . .	} Law Reports, Queen's Bench Division.
Q.B.D. . . . .	
S.C. . . . .	Scottish Session Cases.
Sc. L.R. . . . .	} Scottish Law Reporter.
S.L.R. . . . .	
S.J. . . . .	Solicitors' Journal.
T.C. . . . .	Official Reports of Tax Cases for the Commissioners of Inland Revenue.
T.L.R. . . . .	Times Law Reports.
T.R. . . . .	Taxation Reports.
Ves. . . . .	Vesey.
W.N. . . . .	Weekly Notes.

### OTHER ABBREVIATIONS.

Acct. Tax Suppt. . .	Accountant Tax Supplement.
C.A. . . . .	Court of Appeal.
H.L. . . . .	House of Lords.
Report I.T.C.C. . .	Report of the Income Tax Codification Committee.

All section references are to the Income Tax Act, 1918, unless otherwise stated, *e.g.*, § 14—1936, means Section 14, Finance Act, 1936.

I.T. (Emp), 1943 : Income Tax (Employments) Act, 1943.

I.T. (O. & E.), 1944 : Income Tax (Offices & Employments) Act, 1944.

## FOREWORD

“Income Tax” to-day comprises two charges in the case of individuals : (1) Income Tax at the standard rate, and (2) Sur-Tax, which is an additional Income Tax at graduated rates on the income of individuals in excess of a stated minimum. Throughout this book, the term “Income Tax” is used to denote the charge at the standard rate, as this is the sense in which it is always used, except in legal phraseology.

# INCOME TAX.

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## CHAPTER I.

### THE MACHINERY OF INCOME TAX.

#### § 1.—(a) The Principles of Assessment.

The assessment and collection of Income Tax is founded on a long series of Acts of Parliament the principal of which was passed in the year 1842. The Acts up to the year 1918 were consolidated in the Income Tax Act, 1918, which is the principal Act relating to Income Tax as from the 6th April, 1919.

The rate of the tax is suggested by the Government according to their financial requirements; and variations of the code are also suggested by them according to the experience gained from time to time by the officials, or to introduce innovations which are considered desirable. These rates or variations must, however, receive the sanction of the Legislature before they can be enforced, so that annual Parliamentary sanction is necessary before taxation can be collected.

The Government, having obtained this sanction, are consequently in a position to collect revenue, but the assessment of the taxpayer is in no way within the discretion of the Government. Between the Government and the taxpayer stand the Commissioners, and it is by them that the assessments are determined. The Commissioners hold the scales of justice between the representatives of the Government on the one hand and the taxpayer on the other.

If either the Government or the taxpayer is dissatisfied with the final decision of the Commissioners, the aggrieved party must, where appeal is allowed by the statutes, seek a remedy in the King's Courts.

**(b) Provisions for Continuity.**

Income Tax is not in theory a permanent tax, but is a yearly tax only, imposed by the Finance Act of the year. The Income Tax Act, 1918, as amended by subsequent Finance Acts, regulates the impost when it has been recreated by the annual Finance Act.

Each Finance Act imposes the tax for the year to the 5th April following, when the tax would automatically cease were it not for § 210, 1918, and the Provisional Collection of Taxes Act, 1913. The latter Act continues the existing law for a month from 5th April, to enable the budget resolutions to be passed, and gives statutory effect for a limited period to these resolutions of the House of Commons (in committee) varying or renewing taxation. This avoids the chaos which would otherwise arise between the 5th April and the date of passing the Finance Act for the ensuing year.

Section 210, 1918, provides that as soon as the tax is granted for any year, the provisions of Acts in force as to tax for the year ended 5th April prior to the resolution shall apply to the year for which the tax is so granted. Finally, there are provisions in each Finance Act that that Act shall be construed as one with the Income Tax Acts and all enactments having effect with respect to the Income Tax charged for the previous year continue (as amended by the current Act).

Occasionally, a second Finance Act is passed during an Income Tax year. Where this Act alters the rate of

tax for the year, the new rate so fixed operates for the whole year, any tax already paid by deduction at source being adjusted, as will be seen hereafter.

## § 2.—Board of Inland Revenue.

The general control of the Income Tax is vested in the Commissioners of Inland Revenue who together, or any two of whom, constitute the Board of Inland Revenue. They are appointed by His Majesty, and are subject to the authority, control and direction of the Treasury (The Inland Revenue Regulation Act, 1890).

They have power to appoint officers for collecting, receiving, managing and accounting for Inland Revenue where such officers are not required by law to be appointed by some other authority (*ibid.*, and § 57—1918). The Board advises the Chancellor of the Exchequer and the Financial Secretary to the Treasury on all matters regarding the introduction of amendments of Income Tax law, estimates, etc. They also assess and collect the Profits Tax (§ 24—1937), and the Excess Profits Tax (§ 21—(No. 2) 1939).

## § 3.—Income Tax Officials.

### (a) General or District Commissioners.

General or District Commissioners, who receive no remuneration for their services, were, in 1842, appointed from the Land Tax Commissioners, vacancies in the body being filled up from time to time from a list of persons eligible for the appointment (§ 59—1918). Certain property qualifications are required. In the City of London, the Aldermen and Corporation, the Bank of England, and some other public bodies are allowed to select Commissioners, and in certain

other cities and towns the magistrates and justices may also select a number of Commissioners (§ 59 and 2nd Sch.—1918). The number of General Commissioners in any division must not be less than three nor more than seven, but the Commissioners of Inland Revenue may authorise an increase to a number not exceeding fourteen. The principal functions of the General Commissioners are :

- (1) To appoint a clerk (§ 66) (usually a solicitor or an accountant) who is under their control but paid by the Treasury ;
- (2) To appoint collectors in courts, public departments, and Houses of Parliament, and in the offices of paymasters of civil services (§ 37—1931) ;
- (3) To appoint Additional Commissioners, or to act as such themselves (§ 62, 10th Sch., 1942) ; and to consider cases referred to them by the Additional Commissioners (§ 121) ;
- (4) To allow Income Tax assessments and hear appeals (§§ 121, 122, 125, 126, 133, *et seq.*) ;
- (5) To administer the prescribed oaths to assessors and collectors (§§ 108 (3), 172 (2) (b), 173, etc.) and receive the prescribed declarations of secrecy to be made by Commissioners, clerks, assessors, collectors, inspectors and their assistants (§ 89) ;
- (6) To impose penalties in certain cases (§§ 107, 132).

If an appeal is made to the General Commissioners, their decision on a question of fact is final ; but an appeal against their decision may be made to the High Court on a question of law.

#### **(b) Additional Commissioners.**

The General Commissioners may appoint fit and proper persons to act as Additional Commissioners and any General Commissioner may act as an Additional Commissioner (10th Sch., 1942). Any Additional Commissioner is empowered to form a “meeting” of Additional Commissioners and to do

any act required to be done by Additional Commissioners (*ibid.*).

The principle behind their appointment is that they are presumed to have special knowledge of the different classes of trades and callings in the locality, and they allow assessments under Schs. A, B, D, and E (§ 121—1918; 10th Sch., 1942). Notices of assessment under Schs. D and E are then served on the person assessed, but assessments under Schs. A and B need not be notified to the taxpayer (except in years of revaluation), the demand note being sufficient notice.

**(c) Collectors.**

Collectors are appointed in England by the Commissioners of Inland Revenue except in the cases stated in Chap. I, § 3 (a) (2) (§ 37—1931), in Scotland by the Treasury (§ 85). They are remunerated by the Treasury.

**(d) Clerk to the General Commissioners.**

The clerk is a paid official appointed by them to act as clerk to them and to the Additional Commissioners. In the case of an appeal to the General Commissioners, he gives the appellant information regarding the meeting of the Commissioners for the hearing of appeals, and acts at the appeal in an advisory capacity, attending to all secretarial duties.

**(e) H.M. Inspector of Taxes.**

The Inspector of Taxes is a paid official of the Board of Inland Revenue appointed by the Treasury (§ 75—1918). He issues the return forms, examines returns and prepares assessments and has power to supply omissions, amend assessments and make surcharges,

and certify them to the Commissioners. He also issues the return forms for the Profits Tax and Excess Profits Tax.

All notices of appeals against assessments have to be sent to him. In most cases it is possible to agree the figure of assessment with the Inspector upon presenting proper accounts or other relevant information. In the event of an appeal to either the General or Special Commissioners, the Inspector attends on behalf of the Inland Revenue Authorities, except where the Inland Revenue Solicitor conducts the case. Appeals to the High Court are conducted by the Solicitor to the Board of Inland Revenue in the Inspector's name.

The Inspector can cause additional assessments to Income Tax to be made (§ 125), and in the case of a person who has escaped assessment altogether in any year, the Inspector of Taxes has power (§ 126) to make a supplementary charge, and certify it to the General Commissioners, at any time within six years after the expiration of the year for which the person ought to have been charged. In cases of fraud or wilful default, however, the time limit is abolished in respect of assessments for 1936-37 onwards (§ 33—1942).

#### (f) Special Commissioners.

Special Commissioners are full-time officials appointed by the Treasury (§ 67—1918), and are entitled to such salary and expenses as the Treasury direct. The members of the Board of Inland Revenue are *ex officio* Special Commissioners, but never act as such in making assessments or hearing appeals, confining their acts to those of purely ministerial duties. The taxpayer or the Inspector may call upon the Special Commissioners to state a case on



a question of fact for decision by the Board of Inland Revenue (§ 147). There is no such appeal from the General Commissioners, whose decision on a question of fact is final. On a point of law, an appeal may be made from either the General or Special Commissioners to the High Court, and thereafter to the Court of Appeal and from thence to the House of Lords (§ 149).

The principal functions of the Special Commissioners are—

(1) To assess and charge the Sur-tax, and hear the appeals in connection therewith.

(2) To make assessments under Schedule D and hear appeals thereon in those cases where the taxpayer has elected to be assessed by them instead of by the General Commissioners (§ 123—1918).

(3) To hear appeals, where the taxpayer elects to have the appeal heard by them instead of by the General Commissioners, under Schedules D and E (§ 148—1918; § 19—1922).

(4) To hear appeals in respect of—

- (a) Exemption of the income of charities (§ 37—1918; § 30—1921);
- (b) Claims for repayment of tax on interest paid to banks (§ 36—1918; § 19—1925);
- (c) Questions of domicil, residence and ordinary residence (§ 27—1924);
- (d) Claims for relief on the grounds of error or mistake in returns, etc. (§ 24—1923; § 42—1927);
- (e) Claims for allowances made by non-resident British subjects (§ 24—1920; § 20—1926);
- (f) The valuation of trading stock on discontinuance of trades (§ 26—1938);
- (g) Assessments to Profits Tax where the taxpayer elects to appeal to them instead of to the General Commissioners (S.R. & O. No. 731 (1937)).
- (h) Assessments, etc., with regard to Excess Profits Tax (with certain exceptions) (§ 21—(No. 2) 1939).

(5) To decide disputes as to Life Assurance Allowances under § 32, 1918.

(6) To assess the profits of railway companies and of railway officials under Schedule E.

(7) To assess income from British, Foreign and Dominion Public Revenues under Schedule C.

(8) To determine appeals in respect of Double Tax Relief, and perform other special duties.

Any one Special Commissioner may now act alone to make, sign or allow an assessment (10th Sch.—1942).

Appeals to the Special Commissioners in cases arising in the London District (and in cases arising thereout if so requested) are heard at the Commissioners' Offices, Turnstile House, High Holborn, W.C.1. Special Commissioners also attend periodically throughout the country for the purpose of hearing appeals made to them.

#### (g) Board of Referees.

The Board of Referees are a body of professional and business men appointed by the Treasury for dealing with certain specialised matters. Their offices are at the Royal Courts of Justice, Strand, London, W.C.2.

Their functions are as follows :—

(a) To determine whether there is a *prima facie* case for making a direction under § 21, 1922 in the case of certain companies where the directors have made a statutory declaration that there has been no avoidance of Sur-tax by withholding profits from distribution, and such declaration has not satisfied the Special Commissioners.

(b) To hear appeals under § 21, 1922, from determinations of appeals to the Special Commissioners in connection with directions that the profits of the company be apportioned among the members.

- (c) To hear appeals by or on behalf of any considerable number of persons engaged in any class of trade or business, for the alteration of wear and tear allowances (which must be referred to them by the Board of Inland Revenue) (Sch. D, Cases I and II, R. 6 (6)).
- (d) To fix, on appeal, the percentage of turnover to be adopted in arriving at the profits of a non-resident person chargeable in the name of a resident (Gen. R. 9 (2)).
- (e) To hear certain appeals and consider certain applications, etc., in connection with Excess Profits Tax.

## CHAPTER II.

## THE PRINCIPLES OF INCOME TAX.

## § 1.—Definition and Persons liable.

Income Tax is a levy made by the State on the income arising from sources within the United Kingdom; and also upon the income arising from sources outside the United Kingdom if the person enjoying the income is "resident" in the United Kingdom. If the income arises in the United Kingdom, it is liable to assessment, no matter where the person enjoying it is "resident." The question of what constitutes "residence" is a highly technical one, and will be discussed in Chap. V. The United Kingdom, for this purpose, consists of Great Britain and Northern Ireland.

The liability to Income Tax depends entirely upon the provisions of the Income Tax Acts. There is no question of equity involved in ascertaining whether or not certain profits are assessable.

The following remarks of Lord Cairns emphasise this point :—

"If the person sought to be taxed comes within the letter of the law, he must be taxed, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be. In other words, if there be admissible, in any statute, what is called an equitable construction, certainly such a construction is not admissible in a taxing statute, where you can simply adhere to the words of the statute" (*Partington v. Attorney-General* (1869), L.R. 4 E. and I., App. 100).

Exemption is given to Ambassadors, and other accredited Ministers of any Foreign State, High Commissioners, Agents General, etc., resident in the United Kingdom (Sch. C, Gen. R. 2 (c); § 19—1923; § 26—1925); National Health Insurance Funds (§ 39); and charities satisfying certain conditions (see Chap. IX, § 4).

### § 2.—The Income Tax Year.

The “fiscal year” or “year of assessment” commences on 6th April in one calendar year, and ends on 5th April in the succeeding calendar year (§ 2), *i.e.*, the year of assessment 1947-48 is the year ending 5th April, 1948.

### § 3.—Statutory Income.

Before there can be a charge to Income Tax, there must be a *source* of income, and wherever there is a source of income, the Income Tax Acts lay down rules for measuring the income from that source and charging it to tax. The person in receipt of the income is not normally taken into consideration in the first instance; he comes into the picture only to determine what allowances or reliefs may be granted in charging the tax, or determining whether the source is not chargeable (*e.g.*, because, owing to “residence,” it is outside the purview of the charge), or in charging sur-tax.

In assessing (*i.e.*, measuring) income, the Acts do not in all cases take the actual income of a fiscal year, but rather a statutory income (*i.e.*, the income is measured according to rules laid down by statute).

The statutory income is based upon the actual income arising in the year of assessment from certain

sources, and on the income arising in the year preceding the year of assessment from other sources, according to the nature of the income. There is a statutory income from every source. In general terms, where the actual income cannot be ascertained exactly until it is received and the tax cannot conveniently be deducted at the source, *e.g.*, as in the case of business profits, the income of one year of assessment is measured by that of the previous year, so that the tax may be charged and collected in the year of assessment.

For many purposes, it is necessary to arrive at the "Total Income" of the taxpayer; the TOTAL INCOME for Income Tax purposes means the TOTAL OF THE STATUTORY INCOMES from all sources after deducting the annual charges payable thereout (*i.e.*, annual interest, ground rents, etc.). Although not strictly an "annual charge," bank interest paid also constitutes a deduction if not charged in the taxpayer's Profit and Loss Account.

The tax is to be charged in respect of all property, profits or gains respectively described or comprised in the Schedules marked A, B, C, D and E contained in the First Schedule to the Act of 1918, and in accordance with the Rules respectively applicable to those Schedules (§ 1—1918). These Rules form a code from which is determined the basis to be adopted in respect of each class of income.

#### § 4.—The Rate of Tax.

Tax is levied on the statutory income at a standard rate fixed normally by the Finance Act passed in the year of assessment. In 1945, however, there was a departure from precedent in that the Finance (No. 2) Act, 1945, fixed the standard rate for 1946-7. In the case of

individuals, there is an additional Income Tax called the Sur-Tax, which is levied at graduated rates in respect of incomes in excess of a stated amount (at present £2,000). Sur-Tax is collected on 1st January following the end of the year of assessment, and the rates are therefore normally fixed by the Finance Act of the year following the year of assessment. (Sur-tax is described in Chap. VIII, *post.*) The standard rate for 1946-47 and 1947-48 is 9s. in the £; for the five previous years, *i.e.*, 1941-42 to 1945-46, inclusive, it was 10s. in the £. For rates for earlier years, see Appendix I.

### § 5.—The Five Schedules.

The Schedules contain the Rules for ascertaining the statutory income. Each Schedule deals with a different source—just as a business man, when asked to prepare a statement of his income, would naturally group sources of a like nature together.

There is only *one* Income Tax; the Schedules merely set out the rules for measuring the income from the respective sources, as the basis on which to charge the tax. For facility in collection of tax, assessments are made under the appropriate Schedules, but these assessments are merely parts of the one levy. Students should get into the habit of looking for the source; the Schedule applicable to that source will then provide the rules for measuring the income therefrom.

The Schedules are now explained generally; each is described more exhaustively in later chapters.

**SCHEDULE A.**—Relates to income from the **PROPERTY IN LANDS AND BUILDINGS** in the United Kingdom (*i.e.*, broadly speaking, the income from ownership of land). The assessment is **BASED ON** the

ANNUAL VALUE of the property, less a statutory deduction for repairs, insurance, etc.

SCHEDULE B.—Relates to profits derived from the OCCUPATION OF LAND (*a*) by individuals where the gross annual value of all lands farmed does not exceed £100, or (*b*) otherwise than for husbandry. The assessment is BASED ON the ASSESSABLE VALUE, *i.e.*, in the case of (*a*) THREE TIMES the GROSS ANNUAL VALUE of the land, and in the case of (*b*) ONE-THIRD of the GROSS ANNUAL VALUE.

SCHEDULE C.—Relates to INTEREST AND DIVIDENDS PAYABLE OUT OF PUBLIC FUNDS of the United Kingdom, the Dominions, or any Foreign State where payment is entrusted to any agent resident in the United Kingdom. The BASIS of assessment is the EXACT AMOUNT OF THE INTEREST, etc., paid. (The assessment is on the agent through whom the interest, etc., is paid. *See* Chap. III, § 3.)

SCHEDULE D.—Relates to PROFITS FROM TRADE OR BUSINESS and any OTHER ANNUAL PROFITS OR GAINS which do not come under any of the other Schedules. The BASIS of assessment is, with few exceptions, the PROFITS OR GAINS OF THE YEAR COMPLETED PRIOR to the commencement of the year of assessment.

SCHEDULE E.—Relates to SALARIES, FEES, etc., of all employed persons. The assessment is based on the SALARY, etc., for the ACTUAL YEAR. In all cases, the tax is collected by deduction at source as explained in Chap. III, § 6.

### § 6.—Collection of Tax at the Source.

As has already been stated, wherever there is a source, there are rules for assessing the income arising



from that source. In general, the charge to tax is made at the point where the income first emerges from the source, although the person *assessed* in respect of the income may not be the person who will *enjoy* it, *e.g.*, he may have to pay the income over to someone else in the form of rent, interest on loans, etc. It is, however, more convenient from the Inland Revenue viewpoint to assess the income as soon as it emerges from the source, leaving the person who pays the tax to recoup himself from the person to whom he has to pay such income, by the process of deducting the Income Tax suffered when he pays over the income.

For example, a person who has to pay interest of £20 on a loan is made to pay tax on his income without any deduction for the £20, but when he pays over to the lender the said interest, he deducts tax at the standard rate, thus recouping the tax on that part of his income. He is thus in just the same position as if he had been charged to tax on his income less the £20; the lender is bound to accept the reduced amount in discharge of the interest. The ultimate effect is that the person who enjoys the income bears the tax. Collection of tax at the source is economical and prevents evasion.

The tax under Sch. A is normally collected in the first instance from the tenant, who subsequently deducts from the next payment of rent the amount of tax he has paid on account of his landlord. The landlord is bound to allow this deduction, but in no case can the amount so deducted exceed the standard rate in the £ on the year's rent.

The income from Public Revenues first emerges in the hands of the agent entrusted with the payment of

the interest, annuities, dividends, etc. Accordingly, the agent is assessed under Sch. C and is required to deduct tax on making such payment (Rules of Sch. C). There are exceptions to this rule, however, to save small investors, who are likely to be exempt from Income Tax, from being put to the trouble of reclaiming the tax; also Sch. C does not apply to  $3\frac{1}{2}\%$  War Stock (unless held as bearer securities),  $3\%$  Defence Bonds and certain other securities (*see* Chap. III, § 3). In these cases, unless the holder requires the tax to be deducted before payment (§ 27—1921), the interest is paid gross and assessed under Case III of Sch. D (§ 49—1918 ; § 23—(No. 2), 1931).

The tax in respect of the whole profits of a company taxable under Sch. D is assessed upon the company which is empowered to deduct tax from the dividends paid (Gen. Rule 20 ; § 7—1931).

The person paying annual interest is entitled to deduct Income Tax therefrom at the standard rate (Gen. Rule 19). As will be seen later, in order to maintain the principle of deduction at source, in all cases where the annual charges exceed the income chargeable to tax, the payer of the annual charges must still deduct tax from the whole of the annual charges, and account to the Revenue for tax deducted in excess of the tax he would otherwise pay (Gen. Rule 21). It appears that where arrears of interest are paid and Rule 19 applies, the standard rate applicable when the interest became due must be used (*In re Sebright* (1944), T.R. 243). Under Rule 21, the rate in force at the date of payment is applicable.

Even in the case of annual interest payable to foreigners, the person paying the interest is liable for the tax on the income arising in his hands (except in cases exempted under General Rule 2 of Schedule C) even if the foreigner refuses to allow deduction

from the interest paid thereout. General Rules 19 and 21 apply. If the payer of the interest is not in a position to insist upon the deduction of tax when making the payment he must bear it himself.

The tax on mine rents and royalties, and on royalties payable in respect of patents is also collected at the source. In the case of copyright royalties, however, the tax is collectible at the source only where the payment is to a non-resident and the royalties relate to copies of works not exported from the United Kingdom (§ 25—1927).

The assessment of a partnership is a further example of the principle. The source of income is the business carried on, and the income is assessable in one sum, although in fact it is divisible among the partners. In assessing the firm, effect will be given to the allowances appropriate to the individual partners, but the assessment is made upon the firm, and the obligation for payment rests with the firm. The tax appropriate to each partner is then debited to his Current Account as drawings.

Any agent in the United Kingdom entrusted with the payment of interest, etc., from colonial and foreign companies must likewise deduct and account for tax thereon (Sch. D, Misc. R. 7), as if the interest, etc., were out of Public Revenues.

Where coupons for dividends or interest are sold (apart from the bonds to which they relate) to, or realised by, banks and coupon dealers in the United Kingdom, tax is to be deducted from the proceeds (§ 23—1938).

Where interest and other annual payments are payable to the Crown, the practice is to deduct tax in the same way as if the payment were to an individual.

The principles of deduction of Income Tax at the source are elaborated in later chapters.

Readers must bear in mind the fact that income is only taxed once, usually at the source. A person who receives income under deduction of tax must realise that the tax on that income has already been paid and the income cannot be again assessed in his hands.

Nevertheless, ALL income must be included in the statutory total income from all sources, in order to compute the taxpayer's total liability to tax. He is then given credit for the tax he has suffered by deduction, subject to adjustment for the tax which he himself deducts from annual charges. If he has suffered too much tax by deduction he can claim repayment of the excess.

If a person entitled to deduct tax at the source omits to do so, he is not entitled to recover it from subsequent payments, since payments voluntarily made under a mistake of law cannot be recovered (*see, inter alia, Warren v. Warren* (1895), 72 L.T. 628). The tax may, however, be deducted on payment of arrears of annual payments (*Shrewsbury v. Shrewsbury* (1906), 23 T.L.R. 100), but not in respect of sums already paid (*Hemsworth v. Hemsworth* (1947), T.R. 193). Where tax has not been deducted at source, the recipient of such income cannot claim any repayment, since he has borne no tax thereon.

Where the tax should have, but has not been deducted under General Rule 21 (*see* Chap. IV, § 6), the person receiving the interest can be assessed under Case III of Sch. D (*Glamorgan Quarter Sessions v. Wilson* (1910), 1 K.B. 725; 5 T.C. 537). The Crown has, however, an additional remedy, and can assess the payer. In practice, in such a case a claim is only enforced against the payer for any balance remaining due after the payment of the tax assessed on the payee.

If the interest has been paid out of taxed income, however, the Crown cannot assess the payee.

Where both the payer and the recipient are persons of small means, the Board of Inland Revenue, if so

requested, may allow annual payments to be made without deduction of tax, so as to avoid both the hardship to the recipient involved in his temporary deprivation of the money represented by the tax deducted, and the work and expense involved in unnecessary assessments and claims for repayment of tax. Similarly, the Board will permit insurance companies, etc., to enter into arrangements to pay annuities under deduction of tax at a reduced rate where this will save the recipient from having to make a repayment claim.

### § 7.—Rights of the Individual Taxpayer.

An individual is entitled to certain allowances in arriving at his liability to tax provided he has made a return of his income from all sources, and completed the appropriate claim sections on that return or made a separate claim for the allowances. No such allowances are available for Sur-tax purposes.

A claimant is not entitled to allowance or deduction or relief in respect of any income the tax on which he is entitled to charge against any other person, or to deduct, retain, or satisfy out of any payment which he is liable to make to any other person (§ 17—1918; § 32—1920). He can only get allowances from the income he himself enjoys; all deductible allowances cannot exceed the statutory total income (*cf.* *O'Callaghan v. Newstead* (1940), T.R. 455—see Chap. VIII, § 1).

### § 8.—Earned Income Allowance (§ 15—1925; § 15—1947).

An individual is allowed a deduction amounting to one-sixth (for 1946-7, one-eighth) of his earned income, up to a maximum of £250 (for 1946-47, £150). The

allowance to a married couple is calculated on the total amount of their joint earned incomes, up to a maximum allowance of £250 for the two.

The term "earned income" means :—

- (a) Any remuneration from any office or employment of profit held by the individual ; any pension, superannuation, or other allowance, deferred pay, or compensation for loss of office given in respect of the past services of the individual or of the husband or parent of the individual in any office or employment of profit, or given to the individual in respect of past services of any deceased person, whether the individual or husband or parent of the individual contributed to such pension, superannuation allowance, or deferred pay or not ; and
- (b) The net annual value of any property which is attached to or forms part of the emoluments of any office or employment of profit held by the individual ; and
- (c) Any income which is charged under Sch. B or D or the rules of Sch. D, and is immediately derived by the individual from the carrying on or exercise by him of his trade, profession, or vocation, either as an individual or as an acting partner (§ 14 (3)—1918).
- (d) Any income in respect of Civil List pensions (§ 33—1920).
- (e) Any annuity, pension or annual payment paid to a person, or to his widow or child, or any relative or dependant of his, by the person under whom he held the office or by whom he was employed, or by the successors of that person, notwithstanding that the pension or payment is voluntary (§ 17—1932).

Earned income therefore includes—

- (1) Salaries and wages of employees, however calculated.
- (2) Pensions paid to the individual himself, or to his widow, children or dependants, in respect of his past services.
- (3) Directors' remuneration, including bonuses.
- (4) Income from property taxable under Schedule A where the right to occupy the property

forms part of the emoluments of the office or employment. This is often the case where a clergyman is provided with a vicarage rent free (*see* Chap. VI, § 3).

- (5) Profits from the occupation of farms, etc., whether assessed under Sch. B or Sch. D.
- (6) The business profits of an individual or of an acting partner in a firm.
- (7) Income from patent rights (in the hands of the actual inventor) (§ 40, Income Tax Act, 1945).

The profits of a sleeping partner are unearned income. The precedent acting partner is required to make a declaration in the firm's return as to whether each partner is "sleeping" or "acting." Very slight action on the part of a partner will be sufficient to enable him to be classed as an acting partner.

Unearned income may be regarded as all income which is not included in the above list. This will include—(1) Income from investments; (2) Profits of a sleeping partner; (3) Interest receivable on loans; (4) Income derived from property in land, buildings, etc., except in rare instances.

Where expenses are properly deductible from remuneration (*see* Chapter III, § 5), the earned income allowance must be calculated on the net amount of remuneration after deducting allowable expenses (*Frame v. Farrand* (1928), 13 T.C. 861). Similarly, where the annual charges exceed the unearned income, so that the balance must be paid out of earned income, earned income allowance can only be calculated on the net earned income after deducting the excess charges (*Adams v. Musker* (1930), 15 T.C. 413). The individual can only get allowances from his own income—*i.e.*, from the income he himself enjoys.

#### Illustrations.

- (1) Salary £600, contribution to Superannuation Fund £30.  
The Earned Income Allowance is calculated on £570.

- (2) Salary £400, other Income (unearned) £200, Annual Charges (Loan Interest, etc.) £280. In this case, £200 of the annual charges is regarded as paid out of the £200 unearned income, but the balance of £80 must have been paid out of the salary. The Earned Income Allowance is therefore calculated on  $£400 - £80 = £320$ .

**§ 9.—Old Age Allowance (§ 15—1925 ; § 15—1947).**

It would be an injustice to regard as unearned the income produced by small invested “savings” of old people. Therefore, where a taxpayer or his wife living with him is of the age of 65 or over at the commencement of the year of assessment, and the total income from all sources (including that of the wife, if any) does not exceed £500, the taxpayer can claim a deduction of one-sixth (for 1946-47 one-eighth) of his total income whether earned or not. Marginal relief is given where such a taxpayer’s income slightly exceeds £500, in which case he can elect to pay—

- (a) The amount of tax he would pay if his income were exactly £500 ; plus
- (b) Three-quarters of the amount by which his income exceeds £500.

The allowance granted to a taxpayer in these circumstances is in substitution for earned income allowance, and not in addition to it. The operation of marginal relief is illustrated in Chap. II, § 18 (3).

**§ 10.—Assessable Income.**

This is the sum remaining after deducting from the statutory total income the earned income allowance or the old age allowance, whichever is appropriate.

**§ 11.—(a) Personal Allowance (§ 18—1920 ; § 24—1946).**

A single person is entitled to a personal allowance of £110. A married man who proves that for the



year of assessment he has his wife living with him or that his wife is wholly maintained by him is entitled to a personal allowance of £180. (The position where the wife is separated from her husband is explained in Chap. II, § 21.)

Where a marriage was dissolved by a decree of nullity, the "husband" was held to be entitled to the personal allowance as a married man for the years between the date of the marriage and the decree (*Dodworth v. Dale* (1936), 2 K.B. 503).

**(b) Additional Personal Allowance (§ 18—1920; § 23—1942; § 15—1947).**

If the taxpayer's total income includes any earned income of his wife, the personal allowance is increased by an amount equal to five-sixths (for 1946-47 seven-eighths) of the amount of the wife's earned income, but not exceeding in any case an allowance of £110.

This allowance (commonly misnamed "Wife's Earned Income Relief") does not prejudice the earned income or old age allowance, the intention being that where the wife earns income, the *personal allowance* shall be increased.

The additional personal allowance is not allowed on payments of benefit (*e.g.*, child allowances) under the National Insurance Act, 1946, except on unemployment or sickness benefit or maternity allowances (§ 27—(2) 1946).

In some instances, *e.g.*, in the case of civil servants, under the Superannuation Act, 1935, an employee may arrange for part of his pension to be paid to his wife instead of to himself. At one time this arrangement enabled him to claim the additional personal allowance on the pension paid to his wife, but the allowance is no longer granted in respect of any earned income of the claimant's wife arising in respect of any pension, superannuation or other allowance, deferred pay, or compensation for loss of office, given in respect of his past services in any office or employment of profit (§ 17—1937). The earned income allowance is still allowed on the pension.

The Commissioners can refuse the allowance unless they are satisfied that the wife is actually in receipt of the income, and entitled thereto in her own right (*Thompson v. Bruce* (1927), 11 T.C. 607). This fact is of great importance where a sole trader charges in his accounts a salary paid to his wife.

**§ 12.—Child Allowance (§ 21—1920 ; § 20—1938 ; § 15—1947).**

If the claimant proves that he has living at any time within the year of assessment any child of his who is either under the age of sixteen or, if over that age at the commencement of that year, receiving full time instruction at any university, college, school, or other educational establishment, he is entitled in respect of each such child to a deduction of £60 (previous to 1947-48, £50).

The allowance may also be claimed in respect of a child over 16 who is undergoing training by any person ("the employer") for any trade, profession or vocation, provided that—

(a) the child is required to devote the whole of his time to the training for a period of not less than two years, and

(b) while the child is undergoing the training, the emoluments, if any, receivable by the child, or payable by the employer in respect of the child, do not exceed £13 a year, exclusive of any return of premium. All emoluments receivable by the child, or payable by the employer in respect of the child, are deemed to be a return of premium except to the extent that they exceed in the aggregate the amount of the premium, *i.e.*, until the premium has been returned in full, there are no emoluments.\* The term "emoluments" means any salary, fees, wages, perquisites, or profits or gains whatsoever, including the value of free board, lodging or clothing.

The term child includes a stepchild, but not an illegitimate child unless legitimated by the subsequent

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\* This is for this purpose only ; the child is still assessable under Sch. E on his emoluments which can be taken in cash.

marriage of the parents. Relief is also given for any other child (*e.g.*, an adopted child) who is in the custody of and maintained by the taxpayer at his own expense, provided that no other individual is obtaining the allowance for the same child.

No deduction can be made in respect of any child who is entitled, in his own right, to an income exceeding £60 (previous to 1947-48, £50) per annum, but any income derived by the child from any scholarship, bursary or other similar educational endowment is ignored.

If any question arises as to whether an allowance can be claimed for a child over 16, on the grounds that he is receiving full time education, the Commissioners may consult the Ministry of Education.

Where two (or more) persons are entitled to relief for the same child (*e.g.*, deceased husband and widow, divorced persons, etc.), the allowance is apportioned as the claimants agree, otherwise in proportion to the amount or value of the provision made by them respectively for the child's maintenance and education for the year of assessment. Payments from which tax is deductible are not "provision" for this purpose (§ 24—1940).

**§ 13.—Housekeeper Allowance (§§ 19 and 20—1920 ; § 21—1924 ; § 15—1943).**

(1) A deduction of £50 may be claimed by a WIDOWER (OR WIDOW) who has residing with him either (a) a female relative of himself or of his deceased wife, or (b) if no female relative is able and willing to act, some other female person whom he employs, for the purpose of having charge and care of any child of his (in respect of whom a child allowance is given) OR in

the capacity of housekeeper, provided that no other individual is entitled to a reduction in respect of the same female or, if so entitled, has relinquished his claim, and if the housekeeper is a married woman, her husband has not been allowed the married personal allowance. Not more than one deduction of £50 is to be allowed to any claimant in any one year.

A person employed as housekeeper must be resident with the person claiming housekeeper allowance (*i.e.*, she must sleep in the house) (*Brown v. Adamson* (1937), 2 A.E.R. 792). If the housekeeper is not a relative, she must be *employed*. Employment is a question of fact to be supported by evidence (*MacFarlane v. Hubert* (1936), 19 T.C. 660). A widower cannot claim housekeeper allowance and the personal allowance as a married man in the same year (*Rossi v. Blunden* (1933), 18 T.C. 328).

(2) An unmarried person is allowed the deduction of £50 for a female relative resident with and maintained by him for the purpose of having the care and custody of any brother and sister for whom he is entitled to child allowance, provided neither he nor any other person obtains any other allowance for the same female.

(3) The deduction of £50 for a housekeeper can be claimed by any individual who is entitled to child allowance for a child resident with him, in respect of a female person resident with and maintained or employed by him for the purpose of having the charge and care of the child, provided (a) that he is not entitled to housekeeper allowance in respect of any other person and (b) that no other person is entitled to claim housekeeper allowance for the same female person, and that neither the claimant nor any other person is entitled to an allowance for the female person as a child or dependent relative, or if so entitled has relinquished his claim thereto. (It appears that the housekeeper's husband

could still claim the married man's personal allowance if he is living with his wife, notwithstanding that she is maintained by the employer.) A married man claiming the married personal allowance cannot claim the housekeeper allowance unless he is entitled to child allowance, and throughout the year of assessment his wife was totally incapacitated by physical or mental infirmity. A woman cannot claim the housekeeper allowance, unless she is entitled to child allowance and was incapacitated by physical or mental infirmity, or in full-time employment or engaged full-time in some trade, profession or vocation.

If more than one individual is entitled to this housekeeper relief in connection with the same child, the allowance is apportionable as agreed, or in proportion to the amounts spent in maintaining and educating the child.

Except under (3) above—

A divorced person cannot obtain allowance in respect of a housekeeper (*Kliman v. Winckworth* (1933), 17 T.C. 569).

**§ 14.—Dependent Relative Allowance (§ 22—1920; § 21—1938; § 16—1943; § 15—1947).**

(1) If the taxpayer maintains at his own expense

(a) any relative of himself or his wife, such relative being incapacitated by old age or infirmity from maintaining himself or herself, or

(b) his or his wife's widowed mother, whether incapacitated or not,

he is entitled to a deduction of £50 in respect of the dependant, provided that the total income of the dependant does not exceed £120. If the relative's total income exceeds £70, the allowance is reduced by the excess over £70, *e.g.*, relative's income, £85,

allowance £50, reduced by £85 - £70 = £15 to £35. In other words, the relative's income plus the allowance will always equal £120 where that income exceeds £70. (The taxpayer's contribution, being a voluntary allowance, is not part of the dependant's total income.)

If two or more persons jointly maintain a dependant, the deduction is apportioned between them in the ratio of their respective contributions.

It is the practice to extend the allowance to relatives by marriage.

(2) A deduction of £25 is allowed to a taxpayer who by reason of old age or infirmity is compelled to depend upon the services of a daughter resident with and maintained by him or her. In practice, this allowance is also granted where the taxpayer's wife is incapacitated by old age or infirmity.

It should be noted that there is no residential qualification except in respect of the daughter, but in her case there is no income limit.

(3) An allowance is also given where unemployed members of the household have their unemployment assistance allowances reduced by a portion of the income of another member. To alleviate the grievance that the latter is paying Income Tax on income that is saving the State money in unemployment allowances, it is provided that a person who proves—

- (a) that during any year of assessment he has living with him a relative who in that year has been denied wholly or in part unemployment allowance or public assistance, on the ground that the relative was being maintained wholly or in part by him, and that
- (b) no allowance is granted to him for the relative under (1) above,

shall be allowed a deduction equal to the portion of his income deemed to be contributed to the relative's maintenance, not exceeding £50.

### § 15.—Taxable Income.

This is the sum remaining, after deducting from the assessable income such of the above allowances as are appropriate.

### § 16.—Reduced Rate Allowance.

The first £50 of taxable income is charged to Income Tax at 3s. 0d. in the £, and the next £75 at 6s. 0d. in the £ (instead of at standard rate). The balance of taxable income is charged at the full standard rate.

### § 17.—Life Assurance Relief (§ 32—1918; §§ 26 and 32—1920; § 9—(No. 2) 1940; § 9—1941).

From the tax payable upon the taxable income, a deduction is allowed (in terms of tax) in respect of premiums paid on contracts for life assurance or for certain contracts for deferred annuities on the life of the taxpayer or his wife.

The allowance can be claimed in respect of—

- (a) Premiums (whether annual or not) paid by the claimant or his wife in respect of an assurance, or contract for a deferred annuity, on his own life or on that of his wife;
- (b) Any sum which the claimant is liable to pay, or to have deducted from his salary, to secure a deferred annuity to his widow, or provision for his children after his death.

In the case of (a) the contract must be made with an insurance company legally established in the United Kingdom or in any British Possession, or lawfully carrying on business in the United Kingdom,

or with a registered friendly society, or in the case of a deferred annuity, with the National Debt Commissioners; or the insurances must be made or annuities contracted for with underwriters, being members of Lloyd's or of any other association of underwriters approved by the Board of Trade, who comply with the 8th Schedule to the Assurance Companies Act, 1909 (*i.e.*, have made the necessary deposits with the Board of Trade (§ 20—1932)).

Where premiums in respect of any assurance effected with a registered friendly society are made payable for shorter periods than three months, a person claiming relief must produce a certificate signed by an officer of the society specifying the correct amount of premiums paid during the year of assessment. A person who wilfully gives or produces a false certificate shall forfeit the sum of £50.

The following limitations should be noted :—

- (a) Relief will not be given on that part of a premium which exceeds 7% of the sum payable at death (excluding bonuses, etc.).
- (b) Relief will not be given on that part of the total premiums which exceeds one-sixth of the statutory total income for the year of assessment.  
(From 1941-42 to 1946-47 inclusive, one-sixth of the statutory total income for 1938-39 could be used for this purpose, if that was higher than the total income of the year of assessment (§ 9—1941 ; § 25—1946).)
- (c) If the policy does not secure a capital sum on death, relief will be given only if the policy was taken out not later than 22nd June, 1916, or was effected in connection with certain superannuation or pension schemes. In such a case, relief will not be given on that part of the total of such premiums which exceeds £100.
- (d) The limits of one-sixth of the statutory total income and of 7% of the face value of the policy do not apply in the case of War Insurance Premiums; these are in all cases admitted in full.
- (e) Allowances in respect of life assurance premiums are not granted unless the person claiming is resident in the United Kingdom, except in the case of British subjects, persons in Crown Service, Missionary Service, etc. (§ 24—1920).



- (f) For 1940-41 onwards, no relief is given on any amount by which the allowable premiums exceed the taxable income (§ 9—(No. 2) 1940).
- (g) No allowance can be claimed in respect of premiums on a joint policy; there is only a contribution towards a premium, not the payment of a premium (*Wilson v. Simpson* (1926), 10 T.C. 753). It is, however, the practice to allow premiums on a joint life policy of a husband and wife.

Some life offices will endorse joint life policies of partners, dividing the assurance into two parts, an annual premium being specified in each case, in which case life insurance relief will be allowed to the respective partners.

The relief is calculated on the amount of the allowable premiums paid during the year of assessment, at the rate shown below. For the purposes of life assurance relief for 1940-41 onwards the “standard rate” is fixed as 7s. in the £, for so long as the actual standard rate exceeds 7s. (§ 9—(No.2) 1940).

(This restriction does not apply, however, to compulsory payments under an Act of Parliament or the terms of employment, for the purpose of securing a deferred annuity to the taxpayer’s widow, or provision for his children after his death. Relief in these cases is still calculated by reference to the current standard rate, not the substituted one.)

In the case of policies taken out AFTER 22nd June, 1916, relief is always at half the “standard rate.”

In the case of policies taken out ON OR BEFORE 22nd June, 1916, the rate of relief depends upon the amount of the statutory total income as follows:—

<i>Where the total income</i>	<i>Relief is at</i>
(a) Does not exceed £1,000..	Half the “standard rate.”
(b) Exceeds £1,000 but does not exceed £2,000 ..	Three-fourths of the “standard rate.”
(c) Exceeds £2,000 .. ..	The “standard rate.”

Where a taxpayer elects to apply a cash bonus on his policy as part payment of the premium due,

he is entitled to relief only on the amount he actually pays to the insurance company in the year of assessment (*Watkins v. Jones* (1928), 14 T.C. 94).

Any contribution paid under the National Insurance Act, 1946, is deductible from the income of the payer, and is not treated as an insurance premium.

An allowance of tax was made in respect of compulsory contributions under the Widows' Orphans' and Old Age Contributory Pensions Act, 1925, on £1 as if it were a life assurance premium.

### Illustration.

A's total statutory income for the year 1947-48 was £3,600.

During the year 1947-48 he pays the following premiums in respect of life policies :—

(1) STANDARD ASSURANCE COMPANY—	
Whole Life Policy for £3,000 dated 1911	.. £70
(2) MERCANTILE ASSURANCE COMPANY—	
Whole Life Policy for £12,000 dated 1912	.. £400
(3) LANCASTER LIFE ASSURANCE COMPANY—	
Deferred Annuity Premium—Policy dated 1913	£150
(4) EQUITABLE ASSURANCE SOCIETY—	
(a) Deferred Annuity Premium—Policy dated 1914	£60
(b) " " " " " " 1917	£50
(5) SUN LIFE ASSURANCE COMPANY—	
Endowment Policy for £2,000—dated 1943	.. £180
What relief can A obtain in respect of the above-mentioned premiums ?	
(1 & 2) The First and Second Premiums, viz., £70 + £400, are allowable in full since neither exceeds 7 per cent. of the capital sum assured	.. £470
(3 & 4) The Third and Fourth items must be taken together, and as they amount in the aggregate to more than £100, A can claim an allowance of No part of the £50 premium could be allowed, as policy is dated after 22nd June, 1916.	100
(5) The Fifth Premium is limited to 7 per cent. of the capital sum assured	.. .. . 140
	<hr/> £710

The allowable premiums are restricted to one-sixth of the total income of 1947-48, *i.e.*, to £600, and relief from tax can only be obtained on the latter amount. In such cases, the premiums on the latest dated policies are restricted first, thus giving to the taxpayer the maximum rate of relief available, and therefore the tax deductible in respect of Life Assurance in the Income Tax Assessment for the year 1947-48 will be as follows :—

£570 at 7/- in £ .. .. .	£199 10 0
30 at 3/6 in £ .. .. .	5 5 0
<hr/> £600	<hr/>
Total Tax deductible ..	<u>£204 15 0</u>

NOTE.—An Endowment Policy is one under which a capital sum is payable on a certain date or earlier death, and, since it assures a capital sum on death, the premium thereon is allowed.

*Marginal Relief on policies taken out before 23rd June, 1916 (§ 26 (7)—1920).*

Since, in the case of policies dated not later than 22nd June, 1916, the rate of tax at which life assurance relief is allowed depends upon the statutory total income, anomalies may occur as between taxpayers whose incomes are only slightly different in amount. Thus, with a total income of £1,000 an allowance at only 3s. 6d. in the £ can be made, whereas with a total income of £1,001 the rate is 5s. 3d. in the £.

To obviate these inequalities a “marginal relief” is provided, whereby when the tax ultimately payable by any person, after deducting the allowance in respect of life assurance premiums, is greater than the amount of tax which would be payable if the total income of that person exceeded £1,000 or £2,000, as the case may be, this allowance shall be increased by a sum equal to:

- (a) tax at one-fourth of the standard rate (7/-) upon the amount of the premiums or payment in respect of which the allowance is made, less
- (b) tax at the standard rate (7/-) on the amount by which the total income falls short of £1,000 or £2,000, as the case may be.

An anomaly arises out of the wording of § 32 (9)—1918 (§ 26 (7)—1920), the effect of which is that in applying marginal relief, where the tax payable by the taxpayer with an income just under £1,000 or £2,000, as the case may be, would be more than if the income were over that amount, the additional quarter of the standard rate is allowed on all allowable premiums, and not only on those taken out prior to 23rd June, 1916. The result is that in such cases the taxpayer obtains a greater relief than he would obtain if his income were over £1,000 or £2,000, as the case may be.

## § 18.—Simple Illustrations of Personal Computations.

### (1) General Illustration.

D is a married man with three children under 16. His income consists of a house, of which the Net Annual Value for Assessment is £120, Director's Fees £600, and interest on £900 4% Consols. His wife has a business, the profits of which are £320 for assessment in 1947-48. D pays a premium of £30 on a policy on his own life for £1,200; his wife pays a premium of £20 on a policy on his life for £700. D's own policy is dated 1912, his wife's 1929.

The house is subject to a ground rent of £20 per annum. Mrs. D maintains her widowed mother, who has an income of £75.

### COMPUTATION, 1947-48.

	Sch. A.	Sch. D.	Sch. E.	Total.
	£	£	£	£
House .. .. .	120			120
Director's Fees .. .. .			600	600
Wife's Profits .. .. .		320		320
Interest .. .. .				36
				<u>1,076</u>
Less Ground Rent .. .. .				20
STATUTORY TOTAL INCOME				<u>1,056</u>
Deduct Allowances,				
Earned Income .. .. .		54	100	154
ASSESSABLE INCOME				902
Personal Allowance .. .. .			180	180
Additional Personal .. .. .		110		110
Children (3) .. .. .			180	180
Dependent Relative .. .. .		45		45
		<u>200</u>	<u>400</u>	<u>515</u>
TAXABLE INCOME .. .. .	<u>£120</u>	<u>£111</u>	<u>£140</u>	<u>£387</u>
Chargeable £50 at 3/-; £75 at 6/- .. .. .				
9/- .. .. .	(£120)	£54 0 0 (£111)	£49 19 0 (£125)	30 0 0 (£125)
			(15)	0 15 0 (£202)
Life Assurance Relief—				
£30 at 5/8 .. .. .				38 15 0
£20 at 3/6 .. .. .				147 18 0
		3 10 0	7 17 6	11 7 6
		<u>£46 0 0</u>	<u>£28 17 6</u>	<u>£136 10 6</u>
Payable Jan. 1, 1948 .. .. .	<u>£54 0 0</u>	23 4 6		77 4 6
July 1, 1948 .. .. .		23 4 6		23 4 6
By deduction over year from .. .. .				
April 6, 1947 .. .. .			£28 17 6	28 17 6
By deduction from interest .. .. .				16 4 0
				<u>145 10 6</u>
Recouped from Ground Rent .. .. .				9 0 0
Tax to be borne				<u>£136 10 6</u>

NOTE.—The total column is only shown here to illustrate how the various terms "statutory total income," "assessable income," etc., are employed. Assessments will be made under each of the Schedules as shown in the respective columns.

(2) *Old Age Allowance.*

E is aged 66. He is a widower, having resident with him his sister as housekeeper. His income consists of interest on £10,000 4% Consols and Director's Fees of £80. His life is insured for £1,000 under a policy dated 1910, on which the premium is £29.

## COMPUTATION FOR 1947-48.

Consols Interest	..	..	..	£400	0	0
Director's Fees	..	..	..	80	0	0
				<hr/>		
				480	0	0

*Deduct Allowances—*

Age $\frac{1}{4}$ th	..	..	..	£80		
Personal Allowance	..			110		
Housekeeper Allowance	..			50		
				<hr/>		
				240	0	0

Taxable Income	..	..	..	£240	0	0
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## Chargeable :

£50 at 3/-	..	..	..	£7	10	0
75 at 6/-	..	..	..	22	10	0
115 at 9/-	..	..	..	51	15	0
				<hr/>		
				£81	15	0

*Less Life Assurance Relief—*

£29 at 3/6	..	..	..	5	1	6
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Net Tax to be borne	..	..	..	76	13	6
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<i>Less Tax borne by deduction at source, £400 at 9/-</i>	..	..	..	180	0	0
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Tax reclaimable	..	..	..	£103	6	6
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(In practice, the allowance for earned income, £14, would be given, and old age allowance  $\frac{1}{4}$ th of £400 = £66 for the balance, but the above is legally correct.)

No tax would be deducted from directors' fees.

(3) *Old Age Allowance—Marginal Relief.*

F, whose wife is aged 69, has an income of £510, of which £160 is earned (£40 by his wife). No tax has been deducted at source.

## COMPUTATION FOR 1947-48.

*If Age Allowance is not Claimed : If Age Allowance is Claimed :*

Unearned Income .. £350

Earned Income .. 160

Statutory Total Income c/f. 510

*Less "Margin "* .. £510  
10

c/f. £500

Brought forward	..	£510				£500	0	0
<i>Deduct Allowances—</i>								
Earned Income ( $\frac{1}{8}$ th								
of £160)	..	£27	Age $\frac{1}{8}$ th	£83	6	8		
Personal allowance	180			180	0	0		
Additional Personal								
Allowance								
( $\frac{3}{8}$ ths of £40)		33				33	0	0
		<u>240</u>				<u>296</u>	<u>6</u>	<u>8</u>
Taxable Income	..	<u>£270</u>				<u>£203</u>	<u>13</u>	<u>4</u>
Chargeable :								
£50 at 3/-	..	£7 10 0	£50 at 3/-	..		£7 10 0		
75 at 6/-	..	22 10 0	75 at 6/-	..		22 10 0		
145 at 9/-	..	65 5 0	78 13 4 at 9/-			35 8 0		
		<u>£95 5 0</u>				<u>£65 8 0</u>		
			Add $\frac{3}{4}$ " Margin "			<u>7 10 0</u>		
						<u>£72 18 0</u>		

The claim for Age Allowance would therefore save £22 7s. 0d. in tax.

The tax would be collected partly by deduction under Sch. E (if appropriate), the balance by direct demand.

### § 19.—Exemption of Small Incomes.

Where the total income does not exceed £120, complete exemption from tax is given, whether the income is earned or unearned. Marginal relief applies, so that if the total income exceeds £120 but is less than £135, the tax paid must not exceed one-quarter of the amount by which the income exceeds £120.

#### Illustration.

Total income, 1947-48 (unearned)	..	..	..	£130
<i>Deduct Personal Allowance</i>	..	..	..	110
				<u>£20</u>

Tax thereon £20 at 3/- = £3, but the tax payable must not exceed  $\frac{1}{4}$  (£130 - 120) = £2 10s. 0d. Any tax in excess thereof which has been suffered will be repaid (§19—1935; § 6—1941; § 17—(No. 2) 1945).

### § 21.—Income of Married Women.

The income of a married woman living with her husband is deemed to be his income, and any claim for allowance or relief must be made by the husband, who must include in his return of total income his wife's income as well as his own (Gen. R. 16).

If application is made for the purpose, however, separate assessments\* can be claimed in respect of the income of the husband and the income of the wife. If this is done, separate returns will be made, but the total allowances and deductions granted will not in any case exceed the amount ordinarily obtainable (§ 25—1920), and the *total* tax liability will be the same, the incomes of the husband and wife still being treated as one for the purpose of ascertaining the amount of the total allowances or reliefs deductible.

Section 25, 1920 contains no provision for the case where the proportion of the reliefs which may be allocated to one of the spouses represents more than his or her income. In practice, the balance of the reliefs in such cases is given to the other spouse.

The application for separate assessment must be made either by husband or wife, within six months before the 6th July in the year of assessment (in the case of persons marrying within the year, before 6th July in the following year). The application has effect for that and subsequent years until withdrawn by notice within a like period in the year for which it is desired to revert to joint assessments (Gen. R. 17 ; § 26—1919 ; § 46—1927 ; § 22—1930).

For the purpose of a claim for allowances or deductions, a return may be made by the husband or the wife of the total joint income, but if the Inland Revenue Authorities are not satisfied with such return, they may call upon the other party to the marriage also to make a return.

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\* Separate assessments in respect of Sur-Tax can also be claimed.  
(See Chap. VIII, § 6.)

The apportionments under this section are on the following bases (§ 25—1920; § 46 and 5th Sch.—1927):—

<i>Allowance.</i>	<i>Basis of Apportionment.</i>
Earned Income.	In proportion to— Their respective <i>earned</i> incomes.
Old Age.	Their respective <i>total</i> incomes.
Personal. Additional Personal. Child.	} Their respective <i>assessable</i> incomes.  } Granted to the spouse maintaining the child or relative. If both contribute, the allowance is apportioned on the basis of the contributions.
Adopted Child. Dependent Relative.	
Reduced Rate.	Their respective <i>assessable</i> incomes.
Life assurance premiums.	Relief is given to the spouse who pays the premium.

Where the allowable life assurance premiums are restricted by the operation of the rule relating to one-sixth of the total income, the premiums on policies bearing the latest dates are abated first, thus giving to the taxpayer the maximum relief—the person paying the allowed premium still gets the relief. This is equitable, since relief has always been given on the oldest policies; the fact that a new policy has been taken out should not prejudice the relief on existing policies.

### Illustration.

#### INCOME OF HUSBAND.

Business Assessment, 1947-48	.. ..	£2,000
Gross Taxed Dividends	.. ..	140
Life Assurance Premiums paid by husband—		
On own life (policy dated 1919)	..	£100
On wife's life (policy dated 1910)	..	50
		150

#### INCOME OF WIFE.

Business Assessment, 1947-48	.. ..	£500
Gross Taxed Dividends	.. ..	520
Life Assurance Premiums paid by wife—		
On husband's life (policy dated 1910)	..	100

Claims are made for three children, one adopted child maintained by husband, and wife's widowed mother maintained by wife. The mother has no income.



## COMPUTATION OF INCOME TAX LIABILITY, 1947-48.

## Apportionment.

	Total.		Husband.		Wife.
	£		£		£
Business .. .. .	2,500		2,000		500
Dividends .. .. .	600		140		520
Statutory Total Income ..	3,160		2,140		1,020
Deduct—Earned Income Allowance	250	2,000	200	500	50
		2,500		2,500	
Assessable Income .. ..	2,910		1,940		970
Deduct other Allowances :					
Personal .. .. .	£180				
Additional Personal ..	110				
Own Children (3) ..	180				
	470				
Apportioned 1,940 : 970		£313		£157	
Adopted Child ..	60	60			
Dependent Relative ..	50			50	
	580		373		207
Taxable Income .. ..	£2,330		£1,567		£763
Chargeable—					
£50 @ 3/- : £75 @ 6/-	£30 0 0				
Apportioned 1,940 : 970		(£83)	£10 18 0	(£42)	£10 2 0
2,205 @ 9/- .. ..	992 5 0	(1,484)	667 16 0	(721)	324 9 0
	1,022 5 0		687 14 0		334 11 0
Less Life Assurance Allowance :					
at 7/- .. (150) £52 10 0		(£50) 17 10 0		(£100)	35 0 0
at 3/6 .. (£100) 17 10 0		(£100) 17 10 0			
	70 0 0		35 0 0		
Net tax to be borne	952 5 0		652 14 0		299 11 0
Less Suffered by de- duction at 9/- (£660)	297 0 0	(£140)	63 0 0	(£520)	234 0 0
Payable Sch. D	£655 5 0		£589 14 0		£65 11 0

If no claim is made to be separately assessed, the total column shows the position ; if a claim is made, the separate columns apply. Apportionments should always be made with the assistance of a total column, however, to ensure that the total tax paid is the same as if no claim for separate assessment were made. Allowances are apportioned to nearest £.

Although where the assessment is made on the wife the goods of the wife can be distrained upon for recovery of the Income Tax, the goods of the husband are nevertheless also available for this purpose, but only after failure on his part to pay within seven days of a written demand for payment being made to him or left for him at his usual place of residence (§ 171).

A wife is regarded as " living with " her husband when husband and wife are in intention living together,

although they may be temporarily apart for some reason outside their control, *e.g.*, where the husband is away on business (Report I.T.C.C.).

A married woman, living with her husband (who was not resident in this country), came to this country for from  $4\frac{1}{2}$ — $5\frac{1}{2}$  months each year. She was held to be resident here, but since she was living with her husband, she could only be assessed in his name. Accordingly, no assessment could be raised on her in respect of interest on her holding of War Loan, and since her husband was not resident here no assessment could be raised on him (*Browning v. Duckworth* (1935), 14 A.T.C. 7), except when in this country; if he visited the United Kingdom, he could be assessed when so doing (*Duckworth v. Lowe* (1937), 2 K.B. 560).

A married woman who is living in the United Kingdom separate from her husband can make her own claim for allowances and reliefs applicable to a single person without any account being taken of the income of her husband (Gen. R. 16). A husband and wife are recognised as “living separate” if they are separated under a decree of judicial separation, a separation order, or a properly executed deed. Further, a claim that they are separate is admitted if, when they are living apart by mutual consent or force of circumstances their separation has continued for at least a year and is likely to be permanent. In these circumstances, as from the date of separation, each spouse is treated for tax purposes as an unmarried person (Report I.T.C.C.).

In such cases allowances for children of the marriage are apportionable (*see* Chap. II, § 12).

Where a husband and wife are separated in consequence of the mental incapacity of one of them, the wife is normally regarded as “living with” her husband. If, however, the separation is likely to be permanent, and a claim is made that they are not living together, the wife is treated for all tax purposes as a *feme sole*. Where the wife is treated as a *feme sole*, any allowance paid to the husband or wife out of the estate of the incapacitated person is treated as income of the recipient, and as forming a charge upon the income of the estate (Report I.T.C.C.).

For the year in which the marriage takes place, the portion of the wife's statutory income from 6th April to the date of marriage is treated as her own income as a single person, and the portion from the date of marriage to 5th April following as that of her husband (*C.I.R. v. Brooke* (1923), 8 T.C. 527).

### Illustration.

A lady in receipt of a private income of £1,500 a year marries on 6th May. Her statutory income between the 6th April and 6th May amounts to exactly £100.\* As her income does not exceed £120, she is entitled to claim exemption from Income Tax, and if tax has already been paid by deduction, she can claim a refund of such tax. Her husband will be liable in respect of the balance of the income for the year.

Bearing in mind the fact that assessments are made on incomes from sources measured according to the statutory rules, it will be seen that the amounts of assessments cannot be varied because of marriage; assessments continue to be made on the statutory bases. Once the assessment has been arrived at, however, the marriage affects the machinery of collection. In the year of marriage, all assessments on continuing sources will be "split" on a time basis between the period prior to the date of marriage and the period subsequent thereto. The income for the period prior to marriage will comprise the portions of assessments for that period and all income taxed at source receivable in the period; the total is the income of the wife as a single person. The balance of her income, *i.e.*, for the period since marriage, is deemed to be the husband's income. Neither marriage nor

\* Note that the Statutory Income is not necessarily one-twelfth of a year's income: it will be made up of one-twelfth of all assessments (unless these are for part of a year only), plus the actual dividends, etc., received in the month from 6th April to 6th May.

the death of the husband causes the source to cease to be that of the wife, and the assessments in respect of the income of a married woman living with her husband must be made according to the nature of the source as belonging to the married woman alone (*Leitch v. Emmott* (1929), 2 K.B. 236 ; 14 T.C. 633).

Similarly, when a separation takes place, or the husband dies, the portion of the income of the wife from 6th April to the date of separation or death is treated as the income of the husband, and the portion from the date of separation or death to 5th April as that of the wife. The husband is entitled to the full year's personal allowance as a married man, both in the year of marriage and in the year of separation or his death, although the wife is entitled to allowances as a single woman for the same year.

A widow is regarded as a single person and may claim all relevant allowances as such.

## § 22.—Members of Parliament.

The salary of a Member of Parliament is earned income, and allowance in respect of earned income can be claimed on the net amount after deducting all the expenses wholly, exclusively and necessarily incurred in earning it.

As a matter of convenience, a deduction for expenses of £100 is allowed, unless the Member can prove (as he usually can) that the expenses wholly, exclusively and necessarily incurred by him in the performance of his duties as a Member are more. The expenses allowable are as follows :—

Additional cost of living away from home when engaged in his Parliamentary duties (*i.e.*, either at Westminster or in his constituency).

Cost of travelling between the constituency and Westminster (if not provided by the State).

Secretarial assistance and occasionally rent of office. Miscellaneous expenses necessarily incurred, including stationery, postage, telegrams, and similar items.

When a Member becomes a Minister of the Crown, he becomes the holder of an office for which he receives a salary, and his salary as a Member ceases. Expenses incurred as a Member of Parliament are not allowed as a deduction from the salary as a Minister. Most of the expenses incurred as a Minister are met out of public funds.

### § 23.—Non-Resident Taxpayers and Allowances.

A person who is not resident in the United Kingdom is not entitled to any allowances and reliefs, unless he satisfies the Commissioners of Inland Revenue that he or she—

- (a) is a British subject; or
- (b) is a person who is, or has been, employed in the service of the Crown, or in the service of a Missionary Society, or any Native State under the protection of His Majesty; or
- (c) is resident in the Isle of Man or the Channel Islands; or
- (d) has previously resided within the United Kingdom and is resident abroad for the sake of his or her health, or the health of a member of his or her family resident with him or her; or
- (e) is a widow whose late husband was in the service of the Crown.

If an individual comes within any of these categories, however, it is necessary to compute what his tax liability would be if the whole of his income were liable to Income Tax in the United Kingdom, giving him full allowances as if he were resident here. His liability is then reduced to the proportion of such tax as the income liable in the United Kingdom bears to the total income from all sources (§ 24—1920; § 40—1927), and any excess tax suffered will be repaid.

The Commissioners are empowered by § 28 (3) to receive an affidavit giving the particulars required by the Act and taken before any person who has authority to administer, in the place

where the claimant resides, an oath with regard to any matter relating to the public revenue of the United Kingdom. A consul is the usual person to whom a non-resident turns for this purpose.

An appeal from the decision of the Commissioners of Inland Revenue may be made to the Special Commissioners within three months from the date on which notice of their decision is given (§ 20—1926).

### Illustration.

A is a British subject resident abroad. He has an income from all sources of £2,000 of which only one-quarter is subject to United Kingdom Income Tax (by deduction at source).

Assume A has a wife, two children for whom allowance may be claimed, and one life policy dated 1930, the annual premium upon which is £50. His earned income (earned abroad) is £1,200.

#### COMPUTATION OF LIABILITY, 1947-48.

Income liable to United Kingdom Tax .. ..	£500
Income not liable to United Kingdom Tax—	
Earned .. .. . £1,200	
Unearned .. .. . 300	
	<hr/> 1,500
Statutory Total Income .. ..	2,000
<i>Deduct</i> Allowances—	
Earned Income .. £200	
Personal Allowance .. 180	
Children „ .. 120	
	<hr/> 500
Taxable Income .. .. .	<hr/> £1,500
Chargeable £50 at 3/- .. .. .	£7 10 0
75 at 6/- .. .. .	22 10 0
1,375 at 9/- .. .. .	618 15 0
	<hr/> 648 15 0
<i>Less</i> —Life Assurance Relief—£50 at 3/6 ..	8 15 0
Net Tax to be borne if Total Income	
from all sources were chargeable ..	<hr/> £640 0 0
Proportion applicable to Income liable in the	
United Kingdom $\frac{500}{2000}$ of £640 0s. 0d. =	£160 0 0
<i>Deduct</i> —Tax deducted at source—	
£500 at 9/- .. .. .	225 0 0
	<hr/>
Income Tax repayable .. ..	<hr/> £65 0 0

In these claims, income from those Government securities (*see* Chap. III, § 3) exempted in the hands of non-residents, must be included as income not liable to United Kingdom Income Tax. *See* Chap. X, § 9, as to Dominion Income Tax Relief.

**§ 24.—Due dates for Payment of Income Tax (§ 157) and Interest on Arrears (§ 8—(No. 2) 1947).**

The due dates for payment of Income Tax are as follows :—

- (a) Income Tax payable by all limited or unlimited companies; and by all persons in respect of unearned income, is due on or before 1st January in the year of assessment.

Railway companies in England and Northern Ireland, however, pay tax under Schedule D by four quarterly payments, on or before the twentieth days of June, September, December and March, respectively, in the year of assessment (§ 157 (3)).

- (b) Income Tax payable under Schs. B and D upon the *earned* incomes (and under Sch. A where the income is treated as earned) of individuals and partnerships, is payable in two equal instalments, the first on or before 1st January in the year of assessment, and the second on or before the following 1st July.
- (c) Income Tax payable under Sch. E is deducted at source by the employer who is required to pay it over monthly to the collector (*see* Chap. III, § 5).

Where assessments are made after the due date for payment of the tax, the tax is payable immediately the assessment is signed and allowed.

The special circumstances in which payment of a portion of Schedule A tax may be deferred by a tenant are explained in Chapter III, § 1.

If Income Tax is not paid on its due date, interest at 3 per cent. per annum from the due date to the date of payment is chargeable thereon, but if the tax is paid within 3 months the interest is waived. Where tax is subsequently discharged, the interest is recalculated by reference to the time and amount due, and any overpayment is repaid. Each assessment is treated separately.

No interest is payable :—

- (a) Prior to 1st January, 1948 (*i.e.*, no interest can accrue except from that date or the due date of payment, whichever is later) ;
- (b) if the total tax due on an assessment does not exceed £1,000 ; or
- (c) if the total interest does not exceed £1.

### § 25.—The Necessity for Making a Return.

Every person who receives an Income Tax Return Form is bound under liability to penalties to make a return of his income from all sources (§ 100—1918 ; § 43—1927), and if a person has income liable to assessment to tax, he must give notice to the Inspector of Taxes at or before the end of the year (10th Sch., 1942) even when no Return Form has been received.

A person who does not keep books of account has difficulty in making a correct return ; he should state the fact clearly on the return, and estimate his income to the best of his ability. The taxpayer is clearly in the hands of the Commissioners, who may assess him at whatever figure they please. He has, of course, an opportunity of appealing ; but, as the onus of proof



that the assessment is incorrect falls on himself, the absence of proper books of account will prove difficult to overcome. He will have to satisfy the Commissioners by facts regarding his living and other expenses to show what income must have been available.

The return forms require the taxpayer to state in each case the income of the preceding year. In the Statement of Income must be inserted all income, each type in its appropriate space, according to its source. The statement of ground rent, interest, etc., payable (likewise of the previous year) must also be completed. A space is provided for making notes regarding any changes in sources of income or in interest, etc., payable since the beginning of the previous year. (*See Specimen Return in Appendix III.*)

Since, however, the statutory total income for any year of assessment comprises in respect of certain sources the *current* year's income, particulars of which will appear in the following year's return, it becomes necessary to look at two returns to ascertain the total income for any year.

Thus, in order to arrive at the statutory total income for 1947-48 it is normally necessary to refer to the Returns for 1947-48 and 1948-49, since the figures for income from sources under Schedule D, assessable on the preceding year's income (that of 1946-47) will be found in the 1947-48 Return, whereas income from sources under Schedules A, B, and E, income taxed at source, and charges on income, in respect of which the amounts applicable to the actual year of assessment (1947-48) must be taken into account, will be found in the 1948-49 Return.

The forms issued to individuals also contain sections in which to insert claims for the appropriate allowances,

and those for partnerships, a section in which to show the allocation of the income among the partners.

The return forms are usually issued by the Inspector in April, and must be completed and returned to him within 21 days. Where no completed return is received, the Inspector must make an assessment upon the person chargeable under Schedules A, B and E, in an amount which appears to him to be correct, and estimate the Schedule D assessment for the information of the Commissioners (§ 112—1918; § 46 and 5th Sch.—1927). The assessments are allowed by the Additional Commissioners.

A banker can be required to render returns of untaxed interest received on Government securities belonging to customers but registered in the bank's name, *e.g.*, where the bank acts as trustee under a Will or Settlement, where the stock has been taken as security for an overdraft or a guarantee, etc. (*Attorney-General v. National Provincial Bank* (1928), 14 T.C. 111).

### § 26.—Accounts in Support of Return.

In the case of businesses, the Inspector of Taxes invariably asks for a copy of the Balance Sheet and Accounts in order to facilitate the making of an assessment, and this information should be immediately supplied.

Whilst the Inspector has no legal right to demand accounts, the Commissioners of Inland Revenue can require their production (§ 35—1942), or the Inspector can enforce his demand indirectly and effectively by raising an objection to the assessment, as the Appeal Commissioners can then demand accounts, to which the Inspector must have access. It is therefore wiser

to comply with the request for accounts in the first place. Not only should accounts be submitted, but they ought to be accompanied by schedules shewing the Inspector of Taxes any information that will assist him in his examination of the accounts, *e.g.*, lists of subscriptions; details of any unusual expenses; analyses of repairs and similar items which might include improvements; an explanation of any material variation in the rate of gross profit, or of an expense heading, and so on. He must be placed in possession of all relevant facts; not till then can the taxpayer or his advisers argue any debateable points.

The Revenue prefer that accounts should be certified by professional accountants. If any special points are involved, it is advisable for the accountant to meet the Inspector and discuss the questions freely with him. In this way an agreement will often be arrived at in a few moments which will avoid much future trouble.

Inspectors of Taxes have the responsibility of calculating what is legally due from the taxpayer, no more and no less, and while it may not be the duty of Inspectors to instruct the public as to their rights they go out of their way to do so. It is undoubtedly their business to see that the taxpayer carries out his duties to the State, and in performing this difficult work they are rarely given full credit for the trouble and labour which they take upon themselves for the direct benefit of individual taxpayers.

The queries asked by Inspectors may at times seem unnecessary and irrelevant. It must be borne in mind, however, that the Inspector has not access to the books of account of the client, but may have information not available to the accountant, and the questions are asked in all good faith, and should be

answered accordingly. On the rare occasion when some junior official has been indiscreet, a tactful word to the senior Inspector will be all that is necessary.

### § 27.—Notice of Assessment.

Shortly after an assessment under Sch. D has been made (normally in the autumn), notice is given to the person assessed, who has the right of appeal if the assessment is not, in his opinion, correct. As soon as the notice is received, the amount of the assessment should be checked with the return and with any agreed computations based on accounts, and the allowances verified. Assessments under Sch. E are made in arrear, but are subject to appeal in the same way.

### § 28.—Appeal against Assessment.

If it is decided to appeal, notice must be given in writing to the Inspector within twenty-one days of the date of the assessment notice, the appeal being either to the General or Special Commissioners (§§ 133, *et seq.*), unless the assessment was made by the Special Commissioners, when the appeal must be made to them (§ 147). An appeal must be made wherever the assessment appears to be inaccurate, as the assessment will otherwise become binding.

The Commissioners can allow late appeals where the person concerned has been prevented from giving notice in time by absence, sickness or other reasonable cause (§ 136 (3)). Application in such cases is supposed to be made to the Clerk to the Commissioners, but in practice is made to the Inspector of Taxes.

In his notice of appeal against an assessment made under, or according to the Rules of Sch. D, the appellant must specify the grounds of the appeal. On the hearing of the appeal, he may be permitted to raise another

ground of appeal if its omission from the notice was, in the opinion of the Appeal Commissioners not wilful or unreasonable.

The Appeal Commissioners are bound to hear on behalf of the appellant any accountant who has been admitted a member of an incorporated society of accountants (§ 137—1918; § 25—1923), or any barrister or solicitor (§ 137). In connection with appeals under Schs. A and B, any agent appointed by the appellant must be allowed to plead on his behalf (§ 26—1923).

Notwithstanding that an appeal is pending against an assessment under Sch. D, such part of the tax assessed as appears to the Appeal Commissioners not to be in dispute is to be collected and paid. On the determination of the appeal any balance of tax chargeable in accordance with the determination is payable, or any tax overpaid is repaid (§ 24—1930; 10th Sch.—1942).

Once an appeal has been lodged, the appellant cannot withdraw it; it is the duty of the Commissioners to see that a proper assessment is made (*Rex v. Income Tax Special Commissioners; ex parte Elmhirst* (1935), 14 A.T.C. 509). In practice, he is, however, usually allowed to withdraw it.

The Inspector of Taxes has no more right to be present when the Commissioners are considering their decision than any other party to an appeal (*R. v. Brixton Income Tax Commissioners and Another* (1913), 6 T.C. 195). Accountants attending at appeals should therefore see that the Inspector of Taxes retires with the appellant and his representatives.

If dissatisfaction with the Commissioners' decision is expressed at once, *i.e.*, as soon as they have given their decision, and written notice to the clerk to the

Commissioners is then given within 21 days, accompanied by a remittance of one pound, the Commissioners may be required to state a case on a point of law, for the opinion of the High Court, and the decision of the High Court is subject to appeal to the Court of Appeal and thence (if the Court of Appeal gives permission to carry the appeal further) to the House of Lords (§ 149). Tax in dispute cannot be withheld when the appeal is to the Court; any tax ordered to be repaid will usually bear interest against the Crown.

### § 29.—Production of Books and Accounts in Support of Appeal.

The Commissioners of Inland Revenue or Appeal Commissioners can now compel an appellant to produce Books of Account, Vouchers, etc. (§ 35—1942). The Inspector of Taxes is then entitled to examine, copy, etc., such documents (*ibid*).

If the Commissioners are not satisfied on the evidence tendered that an assessment is excessive, it is within their powers to ask that accounts audited by a qualified auditor be produced as an alternative to immediate confirmation of the assessment (*Hunt & Co. v. Joly* (1928), 14 T.C. 165).

### § 30.—Additional Assessments.

If the Inspector discovers (*i.e.*, has reason to believe) that any properties or profits chargeable to tax have been omitted from the first assessments, or that a person chargeable has not delivered any statement, or has not delivered a full and proper statement, or has not been assessed, or has been under-assessed in the first assessments, or has obtained allowances or reliefs to which he is not entitled, he may amend any assessment under Schedules A, B, D and E which

has not been signed and allowed. If the assessment has been signed and allowed, he must certify the particulars to the Additional Commissioners, who will sign and allow an additional first assessment.

An assessment may be amended, or an additional first assessment be made at any time not later than six years after the end of the year to which the assessment relates, or the year for which the person liable to Income Tax ought to have been charged (§ 125—1918; § 29—1923). In the case of fraud or wilful default the time limit is abolished for tax for the year 1936-37 or any subsequent year and additional assessments may be made at any time (§ 33—1942).

Any adjustment of liability to Income Tax arising from an adjustment of Excess Profits Tax or National Defence Contribution is to be made irrespective of the fact that it may affect a year of assessment for which the above time limit applies (§ 27—(No. 2) 1945).

Where an Inspector changed his mind about an assessment without any new facts having been brought to his notice, he was held to have made a “discovery” enabling him to make an additional assessment (*Williams v. Grundy's Trustees* (1933), 18 T.C. 271). In the Court of Appeal, however, this interpretation of Section 125 (1918), was impliedly, although not expressly, over-ruled in *British Sugar Manufacturers v. Harris* ((1938), 1 A.E.R. 149). The position is thus most unsatisfactory and will no doubt be explored further in some future case in the Courts.

In the case of a deceased person, an additional or amended assessment cannot be made after the end of the third year next following the year of assessment in which the deceased person died, *i.e.*, the assessments

must be made within such three years, but may be in respect of any of the preceding six years in regard to which an assessment can be made (§ 29 (3)—1923), or in the case of fraud or wilful default in respect of any year not earlier than 1936-37 (§ 33—1942).

In the case of interests in the residue of the estate of a deceased person, however, the time within which adjustments of liability of the beneficiaries in the income can be made, is not to expire before the end of the third year following the year of assessment in which the administration of the estate is completed (§ 34—1938).

### § 31.—“Error or Mistake” Claim.

If the taxpayer can show that an assessment under Schedule D was excessive by reason of some error or mistake in the return or statement made by him for the purposes of the assessment, he may, at any time not later than six years after the year of assessment within which the assessment was made, make application in writing to the Commissioners of Inland Revenue for relief. An appeal lies from their decision to the Special Commissioners (§ 24—1923; § 27—1926). The error or mistake must be in the return or statement (*e.g.*, accounts); an error in the basis of assessment through the application of a practice then prevailing is not a ground for relief, even if the Courts have subsequently decided in another case that that practice was wrong.

In determining any such application the Commissioners of Inland Revenue must have regard to all the relevant circumstances of the case, and in particular must consider whether the granting of relief would result in the exclusion from charge to income tax or sur-tax of any part of the profits or income of the applicant, and for this purpose the Commissioners may take into consideration the liability of the applicant and assessments made on him in respect of other years.

Neither the appellant nor the Commissioners of Inland Revenue are entitled to require a case to be stated for the opinion of the High Court otherwise than on a point of law arising in connection



with the computation of profits or income (§ 24—1923), and on no other point (*Carrimore Six Wheelers v. C.I.R.* (1944), T.R. 339).

The above provisions also apply to any assessment to sur-tax (§ 42 (3)—1927), and to assessments under Schedule E (§ 45 (8)—1927). It should be noticed that the relief is in respect of error or mistake in the return or statement made by the taxpayer. Where, therefore, he has made no return and estimated assessments have become binding, he cannot afterwards avail himself of the section to obtain relief.

### § 32.—Post War Credits (§ 7—1941).

There is to be credited in a Post Office Savings Bank account at some date hereafter to be fixed by the Treasury after the war, the additional tax which an individual had to pay by reason of the alteration of the following allowances for 1941-42 to 1945-46 inclusive as compared with 1940-41: Earned income, old age, personal (but not additional personal), exemption limit and marginal relief for small incomes. The maximum Credit for any year is £65. A certificate is issued each year when the tax has all been paid. If either husband or wife apply, the Credit will be divided between them as they agree, or in default of agreement as follows: Credit for earned income allowance in proportion to the respective earned incomes; the balance in proportion to assessable incomes. For 1942-43 onwards, no account is taken of the increase in the additional personal allowance, where applicable, but it is deemed in practice to cancel out the decrease on the earned income allowance of the wife to that extent.

The Credit cannot be assigned, but on death passes to the personal representative for disposal as part of the estate (not liable to death duties on any death prior to the date to be fixed as above).

As the difference between  $\frac{1}{8}$ th and  $\frac{1}{16}$ th is  $\frac{1}{16}$ th, which is  $\frac{2}{3}$ rds of  $\frac{1}{16}$ th, the Credit for earned income allowance is  $\frac{2}{3}$ rds of the new allowance. If that is

added to the reduction in the personal allowance, the Credit is in the ordinary case tax on the resultant total, at the highest rate at which tax is charged.

**Example.**

Married man, income all earned £420, one child.

	1940-41.	1941-42.	Post War Credits.
Total income .. ..	£420	£420	
Allowances: Earned income	£70	£42	£28
Personal ..	170	140	30
Child ..	50	50	
	<u>290</u>	<u>232</u>	
	<u>£130</u>	<u>£188</u>	<u>£58</u>
Chargeable at 6/6 .. ..		£165	£35
„ at 10/- .. ..		<u>23</u>	<u>23</u>
			<u>£58</u>

POST WAR CREDIT.

	Allowance given for 1941-42.	Allocation of Post War Credit.
	£ s. d.	£ s. d.
Earned income or Age allowance	<u>42 0 0</u>	( $\frac{2}{3}$ ) 28 0 0
Personal allowance .. ..		30 0 0
		<u>£58 0 0</u>
Tax as above total	£35 at 6/6 in £ .. ..	11 7 6
	£23 at 10/- .. ..	<u>11 10 0</u>
Post War Credit for 1941-42 .. ..		<u>£22 17 6</u>

Any appeal as to the amount must be made within 3 months of the date of the certificate (Post War Credit (Income Tax) Regulations, 1942 (S.R. & O. No. 1111)).

For 1943-44, any cancellation of tax as a result of the "pay as you earn" legislation, is deducted from the post-war credit of that year (§ 3 (5), I.T. (Emp.), 1943).

In the case of a man aged 65 or over or a woman aged 60 or over, the credits for all years can be claimed on a form obtainable from the Post Office. The payment in these cases will be by direct remittance, not through a Savings Bank Account.

If the title to a post-war credit arises under devolution by will or intestacy, the right to the payment depends on the age of the beneficiary, not of the deceased (§ 26—1946). Other credits are not yet payable.

## CHAPTER III.

## THE FIVE SCHEDULES.

## § 1.—Schedule A.

*(a) Basis of Assessment.*

Under Schedule A, tax is levied upon the net annual value of lands (including the buildings thereon) in the United Kingdom. The tax is popularly known as the Landlord's Property Tax, but it should be remembered that the same rules as regards allowances and deductions apply in the case of income assessable under Schedule A as in the case of income chargeable under any other Schedule. If the allowances to which the taxpayer is entitled are not given against income from other sources, they must be given against the Schedule A assessments.

The gross assessment (called the "gross annual value") is based on the full "rack rent" at which the property is worth to be let in the open market if let on an ordinary yearly tenancy, the rent being the sole consideration for the demise, the tenant paying the usual tenant's outgoings (*e.g.*, parochial and water rates), and the landlord bearing the cost of repairs, insurance, etc. "Worth to be let" means what a tenant could fairly and reasonably be expected and required to pay, taking one year with another.

Where the property is let at a rack rent the amount of which has been fixed by an agreement commencing within the seven years preceding 5th April next before the time of making the assessment, that amount must be taken as the gross annual value. In all other cases it must be estimated, taking into account the

value of similar properties in the vicinity, rating valuations, etc. (Sch. A, Nos. I and IV, 1918; § 28—1930). Where the property is let otherwise than at a true rack rent, the actual rent must be adjusted for any landlord's burdens borne by the tenant, or tenant's burdens borne by the landlord, so as to arrive at what the property would produce if let on the more usual basis. For example, if the occupier undertakes to do all or some of the repairs, an estimated average cost of the repairs (*e.g.*, 10 per cent or 15 per cent., according to the district) will be added to the rent to arrive at the gross annual value. If, of course, the rent is not a fair measure of the worth of the property (*e.g.*, where the property is let on lease at a reduced rent owing to a premium having been paid for the lease, or where a house is let to a relative at a nominal rental), the gross annual value will be estimated.

The valuations normally take place at five yearly intervals (*i.e.*, they are quinquennial valuations), but owing to the War there has been no revaluation since 1935-36.

In ascertaining the annual value no account is to be taken of the value of non-rateable machinery (§ 22—1936), and no regard is to be had to—

(i) any room, etc., added after the building was first assessed to tax or included before it was so assessed, solely for air raid protection, and not used for any other purpose, or

(ii) any structural alterations or improvements made solely for affording such protection,

unless the building or part thereof is let, and the rent or other consideration for the lease is greater than it would have been if no such room, etc., had been added or included or the alterations made.

If the exempted room, etc., becomes used for some other purpose, an additional assessment is to be made.

Any separate unit of assessment intended solely for A.R.P. is to be exempted unless otherwise used or let (§ 17—1938).

Land round a house, not exceeding one acre, is included in the assessment on the house.

*(b) Repairs, etc., allowance.*

Since the gross annual value is fixed on the basis of the landlord bearing the cost of repairs, maintenance, management and insurance, it is only reasonable that a deduction should be allowed from the gross annual value in respect of such repairs, etc. Accordingly, a statutory repairs allowance has been provided (Sch. A, No. V, R. 7; § 27—1942; § 17—1946). The deductions are—

(1) In the case of the assessment upon any house or building (except a farmhouse or building included with lands in assessment):—

Gross value not exceeding £40	..	One-fourth of the gross assessment.
Gross value exceeding £40 and not exceeding £50	.. .. .	£10
Gross value exceeding £50 and not exceeding £100	.. .. .	One-fifth of the gross assessment.
Gross value exceeding £100	.. .. .	£20, plus one-sixth of the amount by which the gross assessment exceeds £100*

(2) In the case of lands (inclusive of the farmhouse if with the land and other buildings, if any): one-eighth of the gross assessment.

Certain expenses are also deductible, *e.g.*, land tax borne by the landlord, certain ecclesiastical dues, drainage rates, and expenses of repairing sea walls.

Under the Tithe Act, 1936, five-sixths of each instalment of any tithe redemption annuity payable in the year of assessment is allowed as a deduction from the annual value for Schedule A. (The deduction in the case of agricultural land is £76 6s. 0d. per cent. and in the case of other land £87 10s. 0d. per cent. of the computed value of the tithe rent charge.)

\* The Net Annual Value can be quickly ascertained in all cases where the Gross Annual Value exceeds £100, from the formula :

$$\text{G.A.V.} - \left( £4 + \frac{\text{G.A.V.} - £4}{6} \right) = \text{N.A.V.}$$

Contrariwise where N.A.V. is over £80,  $\text{G.A.V.} = \frac{5}{6} \times \text{N.A.V.} + £4$ .

The sum remaining after deducting the repairs allowance and any other permissible deductions, is known as the "net annual value," and it is on this sum that Income Tax is levied.

Thus, where the property is let at a rack rent and the tenant pays the local rates, the gross annual value is based on the actual amount of rent paid. The net annual value is that sum, less the statutory allowance for repairs (assuming there are no other allowable deductions).

#### Illustrations.

	£	s.	d.
(1) Annual Rent = Gross Annual Value.. ..	30	0	0
Less Statutory Allowance for Repairs, $\frac{1}{10}$ th	7	10	0
Net Annual Value .. .. .	<u>£22</u>	<u>10</u>	<u>0</u>

	£	s.	d.
(2) Gross Annual Value .. .. .	400	0	0
Less Statutory Allowance for Repairs (£20 + $\frac{1}{10}$ th of £300) .. .. .	70	0	0
Net Annual Value .. .. .	<u>£330</u>	<u>0</u>	<u>0</u>

The assessment upon a house rented at £39 per annum, where the landlord pays the rates, would be arrived at as follows :—

#### Illustration.

	£	s.	d.
Annual Rent .. .. .	39	0	0
Less Rates paid by Landlord (say) ..	14	0	0
Gross Annual Value for Income Tax, Sch. A	25	0	0
Less Statutory Allowance for Repairs, $\frac{1}{10}$ th	6	5	0
Net Annual Value .. .. .	<u>£18</u>	<u>15</u>	<u>0</u>

Where a person occupies his own house, the net annual value is regarded as his statutory income from it and will therefore have to be included as part of his statutory total income.

(c) *Restriction of repairs allowance (Sch. A, No. V, R. 7).*

The quinquennial valuation of property takes into account the facts as they stand at the time. It is not infrequent, however, for the property to be let at a subsequent date on terms that benefit the landlord, and a restriction of the repairs allowance may follow.

The following instances are provided for:—

- (i) *Where the tenant has undertaken to bear the cost of repairs.* In this case, the landlord does not necessarily lose the repairs allowance altogether, but it is restricted, where the rent payable exceeds the net annual value of the property, to such a sum (not exceeding the scale deduction) as will reduce the gross assessment to the rent payable.

**Illustration.**

A house assessed at a gross annual value of £160 is let at £140, the tenant undertaking to bear the cost of all repairs.

The scale deduction would be  $£20 + \frac{1}{3}\text{th of } £60 = £30$ , but this is restricted to £20 so as to make the net annual value £140, the amount of the rent.

If the rent were £120, the full scale deduction would be allowed, making the net annual value £130; and if the rent were £160 or more no repairs allowance would be granted, making the net annual value £160 (the gross amount without any deduction).

- (ii) *Where the rent is considerably in excess of the gross annual value.* In this case, it is necessary to calculate what the net annual value would be if the property was assessed at a gross annual value equal to that rent. If such notional net value exceeds the gross annual value as assessed, no repairs allowance is granted, and the net annual value will be taken at the same figure as the gross annual value

as assessed less any other deductions allowable, *e.g.*, for tithe redemption annuity, land tax, etc. This provision is now of little importance, in view of the assessment of profit rentals (*see* Chap. III, § 1 (*q*)).

#### Illustration.

B is the occupier of a building assessed at a gross annual value of £200, for which he pays a rent of £250.

Since the repairs allowance appropriate to £250 is £20 +  $\frac{1}{8}$ th £(250 - 100) = £45, and £250 - £45 = £205, which is a sum in excess of the gross annual value, no repairs allowance is granted, and £200 is regarded as both the gross and the net annual value.

Had the gross annual value been £210, the repairs allowance would have been given in full, as the notional net annual value is not more than the gross annual value.

#### (d) Valuations.

In estimating the gross annual value, the Commissioners may take into account, in addition to the rent payable, the annual sum which would have to be set aside if a sinking fund were created to replace a premium paid for a lease, with interest (*Davies v. Abbott* (1926), 11 T.C. 575).

The gross assessments under Sch. A are to be made every five years (§ 27—1930), but no revaluation has taken place since 1935-36 (§ 25—1940). An assessment once made and passed by the Commissioners, cannot be increased until the next valuation unless (i) properties have been omitted; or (ii) a person chargeable has not delivered any statement or a full or proper statement, or has not been assessed, or has been undercharged in the first assessment or has been allowed or has obtained any unauthorised deduction, etc., owing to inadequate information at the time of assessment (§ 125—1918); or (iii) there has been any real change in the character of the property itself,



*e.g.*, structural alterations (*Turner v. Carlton* (1909), 5 T.C. 395), such as building a house on the land, or division of the property. In view of the rules regarding profit rentals, however, this has lost much of its interest (*see post* (g)).

On the other hand, the taxpayer may appeal for a reduction in the assessment in any year and not only in a year of revaluation (§ 26—1923 ; § 28—1930).

The net annual value, however, must be assessed each year, since the deductions to be made in arriving at the net annual value may vary from year to year.

A year of assessment for which a revaluation of properties is directed to be made is known as “a year of revaluation,” and the year preceding it is known as a “preparatory year” (§ 27—1930). The last revaluation was made in 1935-36 for the year of revaluation 1936-37. If the annual value for a year of revaluation can be shown to be less than the annual value on which the assessment was based, the taxpayer can appeal for a reduction to the lower value (§ 28—1930).

In the preparatory year the assessors of each district issue to the occupier of each house forms calling for particulars of the rent paid, and other necessary information.

From the decisions in *Klivan v. Stone* and *Hills v. London Freehold and Leasehold Property Co.* ((1936), 20 T.C. 398), it appears that relevant circumstances happening in the preparatory year or the year of revaluation (*e.g.*, a letting at an increased rent) can be taken into account in fixing the annual value, even where the facts become known after the assessment was made, additional assessments being competent under § 125.

In the case of weekly property, it is the practice to have regard only to 50 weeks rent in arriving at the assessment. This gives a valuable concessional relief to cover the extra costs of management, temporary void periods, etc.

(e) *Farms.*

Where the farmhouse is let with the land, the allowance of one-eighth is given from the whole assessment, and the scale deduction for buildings does not

apply. If the farmhouse is let separately from the land, or is occupied by the owner, however, it is not included with the land, but treated for the purposes of the statutory allowance for repairs as a building in the ordinary way, and is therefore subject to the scale allowance for repairs; the allowance of one-eighth is applicable to the land only.

Labourers' cottages on a farm are treated separately from the land, the scale deduction for buildings being given, whether the farm is let or is occupied by the owner.

Glasshouses in market gardens are regarded as buildings.

### Illustrations.

(1) Farm let within preceding seven years at a rack rent of £340, including two labourers' cottages of a gross annual value of £10 each. Land tax £4 and five-sixths of Tithe Redemption Annuity £30, payable by landlord.

Gross Annual Value	..	..	..	..	£340
Less—Tithe Annuity	..	..	..	..	£30
Land Tax	..	..	..	..	4
Repairs—					
Farm, $\frac{1}{8}$ th of £320	..	..	..	..	40
Cottages, $\frac{1}{4}$ th of £20		..	..	..	5
					<hr/> 79
Net Annual Value	..	..	..	..	<hr/> £261

(2) Same facts, save that farm is occupied by the owner. The house is valued at £40 Gross Annual Value.

Gross Annual Value	..	..	..	..	£340
Less—Tithe Annuity	..	..	..	..	£30
Land Tax	..	..	..	..	4
Repairs—					
Farm, $\frac{1}{8}$ th of £280	..	..	..	..	£35
Cottages, $\frac{1}{4}$ th of £20		..	..	..	5
House, $\frac{1}{4}$ th of £40	..	..	..	..	10
					<hr/> 50
					<hr/> 84
Net Annual Value	..	..	..	..	<hr/> £256

(f) *Maintenance Claims.*

The statutory allowance for repairs is in general presumed to cover all expenses in connection with the upkeep of the property and the getting in of the annual income from the property; consequently, no further charges can be made against the net assessment; *e.g.*, where a person owning house property employs an agent to collect the rent, the charges of that agent are deemed to be covered by the statutory deduction. In Scotland, however, owner's rates are deductible in addition to the authorised deduction based on the gross annual value (Sch. A, No. V, R. 4); the net annual value therefore usually varies from year to year.

It may be that the actual expenditure on maintenance, repairs, management and insurance exceeds the statutory allowance. Provision is made in the Acts for increasing the allowance in any year where the owner proves to the satisfaction of the Inspector that his expenditure on repairs, etc., of the property, *according to the average of the preceding five years*, has exceeded the statutory allowance. He can then make a claim for repayment of tax on the excess (Sch. A, No. V, R. 8).

The term "owner" is regarded in practice as including any person who has a beneficial interest in the property, and therefore as extending to a tenant occupying a property at a rent less than the net annual value, or the occupier of a property rent free, or a lessee sub-letting, at an increased rent, a property, the net annual value of which exceeds the rent paid by him.

The year of expenditure can be taken to 31st March or 31st December or any regular fixed date.

It should be noted that this additional relief should take the form of repayment of tax. The allowance will be certified by the Inspector, if he is satisfied as

to the correctness of the declaration made by the owner, and repayment will thereupon be made in accordance with his certificate. If, however, the claim is made in time, the relief is given by reducing the tax payable on the Schedule A assessment.

For the purposes of this relief, the term "maintenance" includes the replacement of FARM houses, farm buildings, cottages, fences, and other works where the replacement is *necessary to maintain the existing rent*; and additions or improvements thereto made in compliance with statutes or bye-laws of a Local Authority where no increased rent is payable (this extends to additions, etc., under the direction of a County War Agricultural Committee).

In comparing the cost of maintenance, repairs, insurance and management of any land or houses with the statutory allowance, the total cost of the repairs, etc., of any land or houses managed as one estate must be compared with the total of the statutory allowances of the whole estate; separate claims for each property will not be allowed. The Revenue attitude towards "one estate" is too narrow; non-urban houses are not necessarily on one estate because they are managed by one agent (*Scottish Heritable Trust Co. v. C.I.R.* (1945), T.R. 97).

If the excess cost of maintenance is greater than the net annual value, the claimant cannot claim repayment on more than the net annual value (*Crompton v. Campbell* (1924), 9 T.C. 224), plus any excess rents (less repairs allowance thereon). This restriction does not apply—for 1946-47 onwards—in the case of agricultural land (§ 32—I.T.A. 1945).

#### Illustration.

Gross Assessment on House, 1947-48	..	..	£80
Statutory Repairs Allowance $\frac{1}{3}$ th	..	..	16
Net Annual Value	..	..	<u>£64</u>

Actual Expenditure on Repairs, Insurance of  
Building and Rent Collection :—

Year ended 31st March, 1943	..	..	£24
do. 1944	..	..	8
do. 1945	..	..	18
do. 1946	..	..	12
do. 1947	..	..	43
			<hr/>
			£105
			<hr/>
Average, one-fifth of £105 =	..	..	£21
Allowance, as above	..	..	16
			<hr/>
Additional Allowance due ..	..	..	£5
			<hr/>

The taxpayer therefore reclaims tax on £5, and his Statutory Income from the house for all purposes for 1947-48 becomes £80 - £21 = £59. It should be noted that there is a new average each year.

Had the average cost of maintenance, etc., been say, £90, *i.e.*, an excess of £74, repayment would only be given on the net annual value (£64); unless the property is agricultural or forestry property the balance of the excess cannot be set-off against other income, except excess rents on the same property.

A claimant who has not had the property for five years must average his expenditure on repairs, etc., with that of the previous owner for the appropriate years, if this is known. In other cases, by concession, the Revenue Authorities permit claims to be made on the basis of the actual expenditure of each year until the five years' average is available, except where dilapidated property has been acquired and large sums spent in its repair, when they usually insist on the average basis only, the previous owner's expenditure (if not known) being taken as "nil." On the first occasion on which a claim on "actual" is made, the claimant is required to give an undertaking to adhere to an "actual" basis until he has a five years' average of his own.

**Illustration of Concession.**

On 30th September, 1942, A. purchased a house assessed at a gross annual value of £80. His expenditure on repairs, etc. (years to 31st March) was: 1943, nil; 1944, £20; 1945, £10; 1946, £28; 1947, £45; 1948, £12. He asked for and was allowed the concession.

Claim :—

	1942-43.	1943-44.	1944-45.	1945-46.	1946-47.	1947-48.
	£	£	£	£	£	£
Actual Repairs, etc.	—	20	10	28	45	12
Statutory Allowances						
( $\frac{1}{2}$ year)	£8	16	16	16	16	16
Excess	—	4	—	12	29	—
Final Net Annual Value for year						
( $\frac{1}{2}$ year)	<u>£32</u>	<u>60</u>	<u>64</u>	<u>52</u>	<u>35</u>	<u>64</u>

For the years in which there is an excess, A will reclaim tax thereon. For 1948-49, he has a five years' average of  $\frac{£115}{5} = £23$ , giving an excess of £7.

It should be noted that in any year in which the actual expenditure is less than the statutory allowance, that allowance is given in full.

No repayment is allowed where the repairs have been allowed as an expense in the computation of profits under Schedule B, Rule 6, or Schedule D.

If, however, a maintenance claim is regularly submitted, an owner-occupier of a farm may charge the gross annual value (one-third of the gross annual value of the house if he lives in it) in his accounts in computing profits, provided no deductions are claimed in the accounts for repairs. This also applies to the farms occupied by an estate owner.

Any claim for repayment operates to reduce the statutory total income of the taxpayer for that year for all purposes, *i.e.*, for allowances and for sur-tax.

There can be included in a claim for maintenance, etc., all repairs, as distinct from improvements, and all costs of maintaining and managing the property, *e.g.*, painting, repairing, etc., the structure, both inside and outside; remetalling drives; repairing fences; agent's commissions and expenses of collecting rents; repairs to heating apparatus; expenses of advertising flats; insurance of the structure; accountant's charges for preparing the claim, etc.

In the case of large estates the claim will also include the wages and employer's contributions to National Insurance of the maintenance staff, the gross annual value of cottages in which the workmen are required to live, pensions to past employees and their widows, subscriptions to local hospital used by the workmen; maintenance and renewals of water supplies, fire mains, lighting plant, heating plant, drains, etc., maintenance of glass-houses, heating apparatus and walls of gardens; cost of running estate office (so far as applicable to management), including gross annual value, and houses occupied by the staff, costs of rent arbitrations, etc., costs of tenancy agreements, stamp duties on owner's copies, advertising for purposes of letting properties, etc. Where home grown timber is used for repairs, the cost of felling, haulage and conveyance, plus the market value of the timber as it stood before being cut, is allowed. Similar principles apply to the cost of getting and carting sand, gravel, etc., used for repairs.

Vouchers in support of the claim are required, and the claim will be admitted either on a cash payments or an expenditure basis, whichever method is adopted consistently. In small cases, the cash payments during the year are normally taken.

Where property is sold, maintenance relief can be claimed in the year of sale in respect of the proportion of the excess of the full average cost of repairs, etc., over the full repairs allowance, up to the proportion of the net annual value of the property for the period of ownership.

**Illustration.**

Gross annual value of estate, £700 ; Repairs allowance, £120 ; Net annual value, £580 ; Average expenditure, five years to 31st March, 1947, £710 ; Property sold 5th January, 1948. The excess of the average over the allowance is (£710 - £120 = £590). Amount available for claim— $\frac{3}{4}$ ths of £590 = £443, but relief restricted to  $\frac{3}{4}$ ths of £580 = £435.

*(g) Abatement of assessment.*

Rule 9 of No. V allows for an abatement of the assessment where a loss has been suffered by flood or tempest, etc. (see Chap. III, § 2 (c)).

*(h) Collection of tax.*

The tax under Schedule A is, in the majority of cases, collected at the source, *i.e.*, from the occupier (No. VII, R. 1), who reimburses himself by deducting the tax paid from the next payment of rent (No. VIII, R. 1 ; § 26—1926).

The landlord is bound, under a penalty of £50, to allow this deduction, upon the production of the official receipt, and any agreement made between the landlord and the tenant, or any clause inserted in the lease, whereby the tenant agrees to forego his rights in this respect, is void (Gen. R. 23 ; § 26—1926). Every person having the use of any lands or tenements is deemed to be the occupier thereof (No. VII, R. 2).

The landlord is not compelled to allow the deduction from any but the next succeeding payment of rent (*Hill v. Kirshenstein* (1920), 3 K.B. 556). If the tax paid by the tenant is not deducted from the next payment of rent, it can be deducted only from any subsequent payment on account of arrears (*Re Sturmev Motors* (1913), 1 Ch. 16).

If no rent is payable for any year, the tax in respect of that year cannot be deducted from the rent of the following year (*Moore v. Drughorn* (1922), 2 K.B. 492).

In any case where the net annual value exceeds the rent, the tenant cannot deduct from the landlord



the whole of the tax he has paid, because the Acts provide that the tenant cannot deduct more than an amount equal to the standard rate in force during the period of accrual on the rent which he actually pays (No. VIII, R. 1).

### Illustration.

X lets his house to his son Y at a rent of £20 per annum. The net annual value of the house is £100, and the tax under Sch. A at 9s. 0d. amounts to £45.

Y cannot therefore legally deduct more than £9 from the rent payable to his father, in spite of the fact that he has paid £45 Income Tax in respect of the property. He enjoys the use of property valued far in excess of what he pays for it, and therefore it is only fair he should himself bear that proportion of tax which relates to his "beneficial occupation." The excess of the net annual value over the rent paid, *viz.*, £80, must be included in Y's statutory total income, and personal and other allowances may be claimed against it to the extent that these are not absorbed by other income.

The position is somewhat anomalous, however, inasmuch as the landlord, although bearing the repairs, does not get the repairs allowance, *e.g.*, if the gross annual value is £124, repairs allowance £24, net annual value, £100, and the rent is £80, the landlord has to bear the tax on the full rent £80 and the tenant on £20. The tenant thus gets the advantage of the full repairs allowance on his beneficial occupation. A claim by a landlord that tax should only be deducted from the rent less repairs allowance (*i.e.*, on the above facts on £80 - £24 = £56) failed (*Egyptian House Properties v. Maynards* (1934), Ch. 681).

In the following cases, the tax is collected from the landlord direct, and not from the occupier:—

- (a) Any dwelling house of an annual value less than £10;
- (b) Any lands and tenements which are let for a period less than one year;

- (c) Any house or building let in different apartments or tenements and occupied by two or more persons severally (the house or building is assessed as one entire house or tenement); or
- (d) Where the landlord elects to have the assessment made on him direct (the election must be made in writing not later than 31st July in the year for which it is first to take effect (Sch. A, No. VII, RR. 8, 9)).

In (a), (b) and (c) above, any person assessed as landlord has to prove that he is not, if that is the fact (§ 12—1941), otherwise he must pay the tax (*ibid.*).

Moreover, any tax so assessed may be recovered by the collector serving on the landlord or any other person who receives any rent paid in respect of the whole or any part of the property (being rent received in the right of the landlord or by virtue of an assignment or mortgage of, or charge on, some right of the landlord in, or on rent from, the whole or part of the property) requiring him to pay to the collector towards the satisfaction of the tax any sums received from time to time on account of rent until the tax is satisfied. Failure to comply with the notice attracts a penalty not exceeding £50 in respect of each payment of rent.

In all the above cases, however, if the landlord fails to pay the tax, it can be levied upon the respective occupiers (No. VIII, RR. 8, 9). In cases (a) and (b), any occupier who pays the tax may deduct it from the next payment on account of rent; and in cases (c) and (d) any occupier who pays the tax may deduct it from the next or any subsequent payment on account of rent (No. VIII, RR. 8-10). No more can be demanded from any occupier, however, than any sum due for rent due at the end of the period during which the demand is made, and a demand cannot be made for rent after the last date on which rent becomes due from him. Any sum so paid by an occupier can be deducted from his next payment of rent. This overcomes the former difficulty of collecting where a large building is let in flats.

The landlord or person immediately entitled to the rent is chargeable in respect of any house occupied by the accredited Minister of any foreign state (Sch. A, No. VII, R. 10). In the case of land or buildings occupied at a rent by the Crown (e.g., by a Government department), it is the practice for the Crown to submit to assessment under Sch. A, and to deduct the tax from the rent.

Any tax payable under Sch. A which is not otherwise recovered may be recovered from the immediate lessor, up to any amount not exceeding tax at the standard rate on the total rents receivable by him for the year of assessment under short leases of the property (being rent payable to, or to the assignee of, the person who was the immediate lessor when the rent became payable).

To facilitate application of the above Sch. A provisions, the inspector or the collector may require any person who is or has been liable to payment (whether on his own behalf or on behalf of another) to furnish particulars of the amount, due dates, and the person to whom he has to pay or account for the rent. A penalty of not exceeding £50 is provided for failure to comply or for rendering false statements. The provisions apply to tax collectible in respect of assessments made at any time, even if before the passing of the Act of 1941 (§ 13—1941).

The tax properly deductible from rent usually exceeds the next payment on account of rent from which it is deductible. To meet this position, the occupier can give notice on Form A/2 to the collector when paying the Sch. A tax that he wishes to pay by two instalments—

- (1) On or before 1st January, the whole tax less the excess referred to; and
- (2) On or before 1st April, the balance. This permits the occupier to deduct the excess from the next succeeding payment of rent (§ 16—1938).

#### Illustrations.

		1947-48.	
		(1)	(2)
Net Annual Value	.. .. .	£60 0 0	£260 0 0
Rent	.. .. .	60 0 0	240 0 0
Tenant pays at 9/-	on £60 ..	£27 0 0	on £260 £117 0 0
And is entitled to deduct from			
landlord at 9/-	on £60 ..	£27 0 0	on £240 £108 0 0
Quarter's rent	.. .. .	15 0 0	60 0 0
Excess which can be deferred until			
1st April, 1948, and deducted	—	—	—
from the following quarter's rent	£12 0 0		£48 0 0

Tenant pays—

1st January, 1948	..	..	£15 0 0	£69 0 0
1st April	..	..	12 0 0	48 0 0
			<u>£27 0 0</u>	<u>£117 0 0</u>

It should be noted that the tenant cannot defer payment of the tax on the value of his beneficial occupation.

(i) *Change of occupier.*

On a change of occupier, the assessment is levied on the occupier for the time being, notwithstanding the change, and the occupier can deduct from rent paid in the usual way.

An occupier who quits occupation remains liable, however, for the tax payable in respect of the period up to the date of his quitting occupation *so far as such tax falls ultimately to be borne by him, i.e.*, where that occupier was the owner or a tenant having a beneficial lease. There cannot be levied upon an occupier tax which ought to have been *levied upon and ultimately borne* by any former occupier (No. VII, R. 3).

An occupier who has had to pay any tax which ought to have been paid by a former tenant or occupier, may deduct it from *any* subsequent payment of rent to his landlord (No. VIII, R. 7).

On a change of ownership of property, it is customary for the tax payable under Schedule A to be adjusted, so that the person who pays the tax or suffers it by deduction from rent received, bears tax only for his period of ownership, *e.g.*, if a person purchased a house in December, the vendor would pay to him tax to the date of completion, so that the purchaser, when he paid the tax for the year, would only suffer his fair proportion.

It may happen that after the Schedule A assessment is made, lands are divided into two or more distinct

occupations. Application can then be made by the persons interested for the charge to be apportioned among the various occupiers (No. VII, R. 5).

Where rent is payable in advance, the rent for the last period of tenancy may have to be paid before the Income Tax becomes due, with the result that the tenant cannot recover the Income Tax because there is no further rent payable. From this there is at present no redress (*British Photomaton Trading Co. v. Henry Playfair* (1933), 2 K.B. 508).

Where lands, etc., are occupied by the owner at the time the Schedule A assessment for the year is made, and he dies before paying the tax, the executors or other persons who become entitled on his death to the rents or profits from the property, are liable to pay the tax for the period up to the time of the death (including any arrears), as well as the tax payable for the remainder of that year, according to their respective interests, without any new assessment (§ 161 (3)).

Only the proportion up to the date of death, however, is income of the deceased. The portion since death is income of the person entitled to the property.

(j) *Annual charges on property.*

Tax is deductible from ground rent and any other annual payments at the standard rate (§ 17—1940).

A mortgagee in possession who has paid tax due under Gen. R. 21 on the mortgage interest, is entitled to charge it in account against the mortgagor (*Hollis v. Wingfield & Ors.* (1940), T.R. 151).

The rent or royalties payable by the lessees under mining leases are treated in the same way as patent royalties, unless the rent is payable in produce, when it is assessable under Sch. D, Case III, on the value of the produce (§ 21—1934).

*(k) Empty Property (voids).*

Income Tax under Sch. A is not leviable on any house which is unoccupied (the furniture must have been removed) for the year of assessment, or in respect of a portion of the year during which it is unoccupied (Sch. A, No. VII, R. 4) unless rent (other than ground rent) is still payable (§ 14—1940). Consequently, any assessment made can, upon appeal, be discharged or diminished by the Commissioners, on due proof of the time during which the house remained unoccupied, except to the extent of beneficial occupation. A house is not regarded as occupied if a servant is living in a room or two merely as caretaker. Relief is also given in respect of unoccupied tenements in houses let in different tenements (§ 21—1930). The relief is extended to waste and unenclosed land. In the case of an otherwise empty factory, the fact that machinery is occasionally “turned over” to prevent rust is not a bar to relief.

Moreover, by concession, the relief is extended to shops, and to rent which is proved to be irrecoverable, lost, remitted or reduced. In the case of lost rent, the relief is tax on the proportion of the gross annual value applicable to the period of loss, but not exceeding tax actually suffered. Where, however, the yearly rent exceeds the gross annual value, the relief is restricted so as to tax the profit rental.

**Illustration.**

Gross Annual Value, £70 ;	Rent, £85, of which £28 has been lost.
Gross Annual Value    £70	Lost Rent    ..    ..    ..    £28    0    0
Rent    ..    ..    85	Restrict by Amount under-
	assessed    ..    ..    ..    15    0    0
Under-Assessment <u>£15</u>	
	13    0    0
	Less for Repairs, $\frac{1}{4}$ th    ..    2    12    0
	Relief allowed on    .. <u>£10    8    0</u>

A further concession allows the discharge of the Sch. A and Sch. B assessments where an owner cannot let land formerly let for husbandry, except as to rent received or other profits or tax on charges. This concession does not apply, if farming operations are carried out, however limited.

A mortgagee in possession is in the same position as the owner in occupation.

For special war concessions, see Appendix XV.

(l) *Landlord's Statutory Income.*

The amount to be included in the statutory total income of the landlord is the net annual value, or the rent received from property let, if this is lower; e.g., if A has three houses, each of a net annual value of £120, one of which he occupies, the other two being let at £140 and £80 respectively, the sums to be included in his statutory total income are £120 for the house occupied, £120 for the house let at £140, and £80 for the house let at £80. For 1940-41 onwards, however, he must also include profit rentals (separately) (*see post (q)*).

(m) *Rent-free Residence.*

Where a person occupies a house rent free, and the annual value of such house can be proved to form part of the emoluments of office or employment of profit (*see Chap. III, § 5*), the net annual value of the property can be regarded as earned income.

(n) *Aerodromes.*

Aerodromes are assessed under Schedule A and B, and (where they are trading undertakings) under Schedule D.

*(o) Sporting Rights.*

The following table, reproduced from the Report of the Income Tax Codification Committee shows clearly the treatment of Sporting Rights:—

Land.	Sporting Rights.	Treatment of Income from Sporting Rights.		
		England and Wales.	Scotland.	Northern Ireland.
Occupied by owner.	Retained by owner.	Included in Schedule A and B assessments on the land.	Not assessed (except in the case of deer forests).	Not assessed.
Occupied by owner.	Let.	Included in Schedule A and B assessments on the land.	Assessed under Case III of Schedule D (formerly No. II of Sch. A).	Assessed under Case VI of Schedule D.
Let.	Retained by owner.	Not assessed (expenses of preserving, etc., regarded as covering value of amenity and any profits).	As in England and Wales.	Not assessed.
Let.	Let to same tenant as the land.	Included in Schedule A and B assessments on the land (even though the land and rights are held under separate leases).	As in England and Wales.	Not assessed.
Let.	Let to different tenant.	Assessed under Case III of Schedule D (formerly No. II of Schedule A).	As in England and Wales.	Assessed under Case VI of Schedule D.

*(p) Schedule A tax on land sustaining war damage (§ 16—1941).*

For 1940-41 onwards, where land subject to a short lease suffers war damage, and in consequence the lease comes to an end or the rent ceases to be payable or is reduced, and the C.I.R. are satisfied that the lessee is unable to deduct tax which he would otherwise have been able to deduct from the rent, the C.I.R. must give him relief (by repayment if necessary) so as to reduce the Sch. A tax ultimately borne by him for the



year of assessment (or part thereof) for which tax is payable to what it would have been if the damage had not occurred. The tax covered by the relief can then be recovered by the C.I.R. from the person who would ultimately have borne it if the damage had not occurred. Tax is deemed to be borne if paid by deduction or otherwise and not deductible from the rent payable.

(g) *Profits Rentals* (" *Excess Rents* ") (§§ 13—17—1940)

(i) *Definitions.*

*Long Lease.*—Lease granted for *term exceeding 50 years* (unless it is for a term of years determinable after the death or marriage of any person).

*Short Lease.*—Any other lease. A lease determinable at the option of the *lessor* before the expiration of 50 years is a short lease. If the *lessee* has the option but the lessor cannot determine the lease within 50 years, the lease will be a long lease.

(ii) *Short Lease Profit Rentals.*

Where an immediate lessor is entitled to rent under a *short lease*, he is chargeable under Case VI on any excess of—

- (a) the rent less any deductions appropriate to a G.A.V. equal to that rent, over the greater of
- (b) the N.A.V., or (c) any rent payable by him under a short lease or leases.

*Example :* Rent received £100, N.A.V. £60 ; Rent payable £70.

Rent .. .. .	£100
Repairs allowance ..	20
	<hr/>
	£80
Less Rent payable ..	70
	<hr/>
Case VI Assessment	<u>£10</u>

If an immediate lessor occupies part of premises or land, the rent received is increased by the annual value of the part occupied. Maintenance claims will be based on the rent (plus the annual value of any part occupied).

In the case of any other short lease, a lessor is chargeable under Case VI on the excess of the rent over the aggregate of—

- (a) the amount, tax on which at the standard rate is equal to the amount of tax under Sch. A in respect of the land which he is liable to pay (by deduction or otherwise);
- (b) the excess (if any) of the rent payable by him for the land under any short lease(s) over the amount referred to in (a);
- (c) any tenants' rates borne by him;
- (d) any relief under Rule 1 or Rule 4 of No. V, Sch. A;
- (e) any tithe annuity borne;
- (f) the cost of services and goods provided under the lease for which there is no separate consideration;
- (g) cost of maintenance, repairs, etc., on a five years' average unless relief is given under some other provision of the Acts.

Compensation payable under the Compensation (Defence) Act, 1939, § 2 (1) (a), for requisitioned property, is deemed to be rent, and the landlord is liable under Case VI for tax on the excess rent (if any) (*Mellows v. Buxton Palace Hotel; Faupel v. Hayward's Exors.* (1943), T.R. 37, 391). Such compensation rent is not necessarily a rack rent so as to be conclusive of the annual value (*Bishop & Marco v. Talbot* (1943), T.R. 267).

**Illustrations.**

(1) A. lets premises assessed at £60 net to B. for £80 per annum. B. in turn, lets them to C. for £120 per annum. Both leases are "short."

	£	
Rent .. .. .	120	
Repairs allowance applicable .. .. .	23	
	<hr/>	
	£97	
<i>Deduct</i> rent paid, being greater than N.A.V.	80	
	<hr/>	
Excess rent assessed on B. .. .. .	£17	(Case VI)
	<hr/>	
Rent receivable .. .. .	80	
<i>Less</i> N.A.V. .. .. .	60	
	<hr/>	
Excess rent assessed on A. .. .. .	£20	(Case VI)

(2) Had the N.A.V. been £90, B. would have been assessed on £7, but A. would not have been assessed in respect of excess rent, as B. would have been entitled to deduct tax on £80 when paying his rent to A. B. would be in "beneficial occupation" of £10.

It will be seen that the real value of the property is spread according to the enjoyment of it :

		(1)	(2)
A.—by deduction on .. .. .	£60		
Case VI on .. .. .	20	80	80
	<hr/>		
B.—by deduction on .. .. .	£60		90
Case VI on .. .. .	17		7
	<hr/>		
	£77		£97
<i>Less</i> Recouped by deduction on .. .. .	60	17	80
	<hr/>		
		£97	£97

(3) Inclusive rent from a group of short leases £500 ; N.A.V. £300 ; Rates £60 ; excess of maintenance claim over repairs allowance £30.

Rent .. .. .	£500
<i>Deduct</i> N.A.V. .. .. .	£300
Rates .. .. .	60
Maintenance .. .. .	30
	<hr/>
	390
	<hr/>
Excess Rent .. .. .	£110

(iii) *Long Lease Profit Rentals.*

In the case of long leases, Gen. Rules 19 and 21 apply to annual sums payable, and if not otherwise charged, such payments are chargeable under Case VI. Relief is given to charities, hospitals, etc., as if Sch. A still applied.

§ 2.—**Schedule B.**

(a) *Basis of Assessment.*

Prior to 1941-42, persons occupying lands were in a privileged position, inasmuch as they were assessed under Sch. B, not on the profits they made from the occupation of the land, but on a statutory profit measured by the rental value of the land. Farmers need not therefore produce accounts unless they wanted to depart from the statutory basis of assessment because their actual profits were less. If their true profits were more, they could not be assessed on the excess. For 1941-42, the larger farmers, and for 1942-43 onwards, all except the smallest, have lost this privilege (§§ 10, 11—1941, § 28—1942).

Under Sch. B, tax is now levied in respect of the occupation of (a) all lands not occupied wholly or mainly for husbandry, and (b) farm lands and buildings occupied for husbandry by an individual or partnership and not exceeding £100 gross annual value (for 1941-42, £300). Dwelling houses with not more than one acre of garden (other than the farmhouse attached to the farm land) and business premises are excluded from Sch. B.

For 1941-42 onwards, market garden land (*i.e.*, land occupied as a nursery or garden for the sale of the produce, other than land used for the growth of crops) formerly assessed under Sch. B but according to the

Rules of Sch. D, is charged under Sch. D in all cases. Moreover, where a person farms land or lands, the farm profits will be charged under Sch. D, Case 1, and not under Sch. B, except in the case of an individual where the total gross annual value of all farming land (including the farmhouse and buildings) occupied by him (including his share of lands farmed in partnership) does not exceed for 1941-42, £300, and for 1942-43 onwards, £100. Where the farmhouse is assessed under Sch. A separately from farm land, its gross annual value must be added to the gross annual value of the land for this purpose. Woodlands and kitchen garden may be omitted in considering whether the total farm land exceeds £100 (*De Poix v. Chapman* (1947), T.R. 399).

A partnership farming lands of a gross annual value exceeding these limits is assessable under Sch. D no matter what the circumstances of the partners may be (§§ 10, 11—1941; *C.I.R. v. R. & J. Houston* (1943), T.R. 89). Moreover, even if the partnership farms lands of less than the annual value mentioned, it will be assessed under Sch. D, unless *all* the partners as individuals escape Sch. D under the provisions mentioned above. All land farmed by a company is assessable under Sch. D no matter what the value.

If the land is “farm land” for only part of a year, it will be charged as such for that part, the charge for the remainder of the year being under Sch. B as before. For this purpose, apportionments of assessable value must be made in months and fractions of months.

The assessment under Sch. B is based upon what is called the “assessable value,” *i.e.*, for 1942-43 onwards, three times the gross annual value (prior thereto the gross annual value), unless the lands are not wholly

or mainly occupied for the purpose of husbandry (*e.g.*, woodlands, parks and amenity lands occupied with the mansion house and not used for husbandry, gardens and pleasure grounds; moorlands; land used for rearing game; golf courses; football and cricket grounds; sewage farms; silver fox farms, etc.), when the assessment is upon one-third of the gross annual value.

All farming carried on by one person or partnership or company is treated as one trade carried on by him or them. Assessments for the year (1941-42 or 1942-43) in which compulsory Sch. D assessment first arose were made as if farms had always been assessed under Sch. D, *i.e.*, a farm was not regarded as a new trade simply because it came under Sch. D for the first time, and if losses had been incurred in the preceding six years, relief under § 33, 1926, or § 29, 1927, had to be given on the amount that would have been available for relief if the assessment had always been under Sch. D, appropriate balances being carried forward.

A transitional relief was given for the year 1941-42 or 1942-43, whichever was the first to which compulsory assessment under Sch. D applied, on a claim being made within 12 months from the end of the year in question. If an individual or partnership of individuals proved that the actual profits of that year were less than the assessment thereon, claim could be made to have the assessment reduced to the actual profits. This applied to surtax as well as to income tax. It will be noted that this relief did *not* apply to a company.

In deciding whether a farmer is assessable under Sch. D, it is necessary to aggregate the gross annual value of all his farm and market garden land with so much of the annual value of any such land of a partnership of which he is a member as is proportionate to his share in the partnership income. If in the

relevant period (*i.e.*, the twelve months preceding the year of assessment, or if the individual in question began farming in the year of assessment, that part of the year of assessment during which he was farming) the total annual value does not exceed £100 (1941-42, £300), he will continue to be assessed on farming under Sch. B; the market garden portion will be assessed under Sch. D.

The preceding paragraph applies to a partnership as it applies to an individual, but not if any of the partners carries on farming in the year of assessment in such circumstances that he is assessed under Sch. D.

#### Illustration.

A and B farmed the following lands :—

- (1) A, land valued at £50; (2) B, land valued at £100;
  - (3) A and B, in partnership, land valued at £90 (equal partners).
- For 1942-43 onwards :—

A is farming land valued at  $£50 + \frac{1}{2}$  of £90 = £95, and is therefore assessable on his own farm at  $£50 \times 3 = £150$  under Sch. B.

B is farming land valued at  $£100 + £45 = £145$ , and is therefore assessable under Sch. D on his own land on the profits of the preceding year.

The partnership is assessable under Sch. D, as one of the partners is assessable under Sch. D.

For 1941-42, all would be assessable under Sch. B on the gross annual value.

If for any year of assessment an individual or a partnership of which an individual is a member is assessed under Sch. B, he or they will not be allowed any relief under § 33, 1926, or § 29, 1927, in respect of any prior loss.

It will be seen that the assessment under Sch. B is based on a statutory income which has no direct connection with the actual profits which the occupier of the property may make. Thus, where the gross annual value of a farm is £100, three times that amount,

or £300 is regarded as the profit of the occupier of the farm and constitutes his statutory income derived from the occupation of the farm (§ 23—1922, § 28—1942).

A small farmer is thus regarded as making a profit equal to three times the rent he pays for the farm, irrespective of what actual profit he makes, unless he makes a special claim to be assessed by reference to his actual profits (*see infra*).

Where a person both owns and occupies a farm, he will pay Income Tax thereon under both Schs. A and B or D. He will pay tax under Sch. A on the *net* annual value in respect of the income deemed to accrue from the ownership of the farm, and if his gross annual value does not exceed £100, under Sch. B on three times the *gross* annual value in respect of the profits deemed to be derived from working the farm, otherwise under Sch. D on the profits shown by his accounts.

For the purposes of Sch. B, the gross annual value of the land includes the value of the farmhouse and buildings occupied for purposes of husbandry (§ 10 (2)—1941). The gross assessment for Sch. A determines the basis of the assessable value for Sch. B.

As to sporting rights, *see* Chap. III, § 1 (o).

The valuations for Sch. B are made at the same time as those under Sch. A, under similar rules (except that no deduction from the gross annual value is made). Consequently, where the rent is increased between two valuations, the Schedule B assessment cannot be increased until the next revaluation, unless any material improvement has been made in the way of farm buildings, or the acreage of the farm extended. If, however, the rent is lowered, application should be made for a reduction in the assessment.



(b) *Claims for Adjustment of Schedule B Assessments.*

A person assessed under Sch. B on lands occupied for husbandry has the valuable option that for any year in which he can prove that the actual profits from working the farm are less in amount than the Sch. B assessment, he can claim to have the Sch. B assessment reduced (for that year only) to the actual profits ; and if tax has already been paid in full, a claim for refund of tax can be made in respect of the amount overpaid (Sch. B, R. 6). The claim must be made within one year after the end of the year of assessment to which it relates (§ 30—1923).

A farmer assessed under Sch. B need not produce accounts except to support a claim under Rule 6, or under § 34, 1918, where a loss is made, or if he should happen to be liable to Profits Tax or E.P.T.

As to stock valuations, *see* Chap. IV, § 4.

(c) *Relief for Flood and Tempest or Agricultural Depression.*

Relief is granted to the occupiers of agricultural land, where owing to flood or tempest the whole or a portion of the lands is rendered unfit for cultivation, or loss has been sustained to growing crops or stock on the land. The Commissioners, on satisfactory proof that the owner has abated any portion of the rent, may reduce the assessments under Schedules A and B accordingly. If the owner is in occupation, the Commissioners may abate the assessment to such an extent as they consider would have been appropriate if a tenant had been in occupation (Sch. A, No. V, R. 9. ; Sch. B, R. 3.). In addition relief is given as a concession, in cases where, owing either to agricultural depression generally or to the farming difficulties of a particular tenant, a temporary

remission of rent in money is made by a landlord without consideration for such remission.

(See Chap. III, § 1 (*k*) for concession where land cannot be let.)

(*d*) *Woodlands.*

These may, at the option of the occupier, be assessed under Sch. D, instead of Sch. B, provided they are managed on a commercial basis and with a view to the realisation of profits. The election to be assessed under Sch. D must extend to all woodlands so managed on the same estate, except that woodlands which are freshly planted or replanted may be treated as being on a separate estate if the occupier gives notice accordingly to the Commissioners within ten years (§ 23 (2)—1922) after planting or replanting. Once the occupier has elected to be assessed under Sch. D, he continues to be so assessed. Assessment under Sch. B will not again arise until a change in occupier takes place (Sch. B, R. 7).

So long as no election has been made, the woodlands remain assessable under Sch. B, on one-third of the Gross Annual Value, and the profit resulting from the sale of estate timber is covered by that assessment (*Christie v. Davis* (1945), T.R. 63).

(*e*) *Losses.*

A farmer who sustains a loss in any year is entitled, upon giving notice to the Inspector of Taxes within one year after the year of assessment, to apply to the General Commissioners for a repayment of tax on the amount of the loss under § 34, 1918 (see Chap. VII, § 2). If assessed under Sch. B, he will also claim a reduction of the Sch. B assessment to the actual profit for the year, *viz.* nil, under Rule 6, so as to leave

the whole loss available under Section 34 for a claim for repayment of tax suffered on other income. If, however, he is assessed under Sch. D, the original Sch. D assessment for the year will stand, and the loss must first be set against that assessment, and only the balance of the loss (if any) will be available against other income.

A farmer assessed under Sch. D who has suffered a loss in respect of which relief has not been wholly given under any other provision of the Acts, can carry forward the loss (or so much of it as remains available), to be deducted from the next assessment on the same source under Sch. D, during the succeeding six years. If, however, he ceases to be assessable under Sch. D (*e.g.*, by reduction of the gross annual value to £100 or less), no further deduction or set off in respect of the loss sustained can be claimed (§ 33 (4)—1926; § 28—1942) (*see* Chap. VII, § 2). Likewise the carry forward of a wear and tear allowance after a return to a Sch. B assessment is not allowed.

(f) *Cattle Dealers and Milk Sellers.*

As to the profits of cattle dealers and milk sellers in excess of the Sch. B assessment, where the Commissioners consider that that assessment affords no just estimate of the profits, *see* Sch. D, Case III (*see* Chap. V, § 1). This has now little application.

(g) *Bank Interest Paid.*

Although the ordinary Sch. B assessment is presumed to cover the whole of the normal farming operations, a claim can still be made under § 36, 1918, for repayment in respect of interest paid to a banker, etc. (*See* Chap. IX, § 6.)

(h) *What Constitutes "Husbandry."*

" 'Husbandry' is a term of very wide signification . . . the question whether a man is engaged in husbandry is very much a question of fact and of degree . . ." (Sankey, J., in *C.I.R. v. Ransom & Son* (1918), 2 K.B. 709). "Lands . . . are occupied for husbandry if the trade or business carried on by the occupier depends to a material extent on the . . . use of the fruits . . . of the lands . . ." (Clyde, L.P., in *Lean and Dickson v. Ball* (1926), S.C. 15). Poultry farming was held to be husbandry (*Lean and Dickson v. Ball, supra*). In *Back v. Daniels* ((1924), 9 T.C. 183), a firm of wholesale potato merchants grew some of their produce on lands hired from farmers for seasonal periods, where they provided the seed, some manure, and the labour for planting and lifting the potatoes, but the farmer ploughed and cultivated the land and carted the potatoes (paying rent, rates and taxes); it was held that the firm had the use of the land, and were assessable under Sch. B. (This would now apply only if the gross annual value of all lands did not exceed £100.)

Sheep grazing is just as much husbandry as tillage or cultivation of the soil (*Keir v. Gillespie* (1919), 7 T.C. 473). Where, however, additional land is rented on what is known as the "eleven months' " system, the graziers may be assessed under Schedule D, Case VI (*McKenna v. Herlihy* (1920), 7 T.C. 620); the person letting the land is still the "occupier" and assessable under Sch. B or D (as may be appropriate) (*C.I.R. v. Forsyth Grant* (1943), T.R. 233). The principle underlying this case is that the farmer is really selling the growing grass. The Sch. B assessment does not cover profits arising from things done outside the farm (*Donald v. Thomson* (1922), 8 T.C. 272),

unless the arrangement is an ordinary incident in the conduct of the business as a farmer, *e.g.*, the Sch. B (or D) assessment covers the profit made on sheep which are, according to the custom of the district, wintered on lands in less exposed districts (*C.I.R. v. Marshall and Mitchell* (1928), 14 T.C. 341). Likewise, an out-and-out letting, even under a verbal lease and for less than a year, of the lands themselves to a tenant who is entitled to use the lands in any way he likes, and not merely for grazing, makes the tenant the occupier (assessable under Sch. B or D as is appropriate) (*Mitchell v. C.I.R.* (1943), T. R. 241).

Where lands are occupied exclusively for the purpose of breeding racing stock, the occupation for this purpose falls within the scope of Sch. B (where the gross annual value does not exceed £100). The use of stallions, whether for serving the mares of the occupier or outsiders, is an ordinary part of the activities of a breeding establishment, and the fees received for the services of stallions *on the lands* are covered by the assessments under Schedule B. If, however, the lands are occupied as an ordinary farm (even if breeding is an incident of the farming), and the services of the stallion are employed *outside* the lands, *e.g.*, where it is let out and taken round the country, the fees are assessable under Schedule D, Case VI (*Glanely v. Wightman* (1933), 12 A.T.C. 209).

Similarly, profits arising from the sales of the progeny of a brood mare kept on a stud farm arise from the occupation of land under Schedule B (*Dawson v. Counsell* (1937), 3 A.E.R. 248).

Where a farmer plants willows with a view to commercial profit, he is assessable upon the profits derived from the sale of the willows as part of his

profits as a farmer. Where, therefore, he is assessed under Sch. D, such sales must be credited in his accounts (*Elmes v. Trembath* (1934), 19 T.C. 72).

Silver fox farming has been held to be assessable under Schedule B, but on one-third of the annual value, as the land is not occupied for husbandry. The Court held that they could not interfere with the decision of the General Commissioners on the point of fact (*C.I.R. v. Melross* (1935), 19 T.C. 607).

### § 3.—Schedule C.

Under Schedule C, tax is levied in respect of all profits arising from interest, annuities, dividends and shares of annuities, payable to any person, body politic or corporate, company or society, OUT OF ANY PUBLIC REVENUE. This includes interest and dividends payable out of public funds of the United Kingdom, Dominions and British Possessions, or of any foreign state, where the payment of interest is entrusted to an agent resident in the United Kingdom. Where interest on such securities is paid gross, the income is assessable under Schedule D, Case III or Case IV (as may be appropriate).

The expression “public revenue” includes the public revenue of any Government whatsoever, and the revenue of any public authority or institution in any country outside the United Kingdom (§ 23 (3)—1938).

It must be observed here that the income first emerges from the source in the hands of the agent, and the income is accordingly assessed in his hands. The basis of assessment is the actual income from the source during the year of assessment.

The agent entrusted with the payment of the interest, etc., is required to deduct the tax from the

interest or dividend, and to pay such tax into the general account of the Commissioners of Inland Revenue at the Bank of England. If the interest, etc., is on stocks, etc., of a foreign state or British Possession and is payable to a person not resident in the United Kingdom, tax is not charged, as the recipient is not liable (Sch. C, Gen. Rule 2 (*d*)). Where a banking business, assurance business or security-dealing business is carried on in the United Kingdom by a non-resident, the exemption of interest, etc., granted by Rule 2 (*d*) of the Gen. Rules, Sch. C, does not apply. Moreover, where such a business is carried on in the United Kingdom by a person not ordinarily resident therein, and any income from Treasury securities (*e.g.*, 3½% War Loan, see below) is excluded from profits by virtue of the conditions of issue, any interest on money borrowed for the purpose of acquiring the securities, and any other expenses attributable to the acquisition or holding of, or to any transaction in, the securities, must be excluded in computing profits (§ 21—1940).

The Governor and Directors of the Bank of England are Commissioners for the purpose of assessing their own profits, and also in respect of dividends, interest, annuities, etc., payable out of the public funds, which are entrusted to them for payment.

Where the half-yearly amount of any interest payable out of the public funds does not exceed 50s., the interest is paid gross, no tax being assessed under Schedule C, unless the stock is held in bearer bonds so that the interest is paid on coupons (Sch. C, Group 2, R. 9.). In the case of 4% Victory Bonds, however, tax is always deducted at source.

The interest on stock standing in the name of the National Debt Commissioners, *e.g.*, the Post Office Register account; the Savings Bank fund; the Post Office Savings Bank fund; the Friendly Societies fund; various funds under the National Health Insurance Acts; the Supreme Court deposit and exchange account;

the Irish Land Purchase Fund is paid to the National Debt Commissioners without deduction of tax and so passed on to the accounts concerned.

Where tax is not deducted at source, the interest is assessable under Schedule D.

Interest, dividends, etc., payable out of the revenue of foreign states, which are not entrusted for payment to any agent resident in the United Kingdom, cannot be taxed under Schedule C. The recipients are therefore called upon to declare such profits in their Income Tax returns for assessment under Schedule D, Case IV.

Under Schedule C, the rate of tax is determined by the date of payment, and not by the rate or rates in force during the time the interest accrued (§ 39—1927).

From the viewpoint of the recipient of income taxed under Schedule C, the income has been taxed at source; the gross amount must be included in his return of total income, credit for the tax paid being taken in arriving at the amount of tax remaining to be paid or reclaimed.

In the case of the  $3\frac{1}{2}\%$  War Stock, the interest (except on bearer bonds) is paid gross without deduction of tax (§ 49—1918; § 23—(No. 2) 1931), unless an application to have the interest paid less tax has been made (§ 27—1921). The recipient is assessable in respect of such interest under Schedule D, Case III, on the basis of the amount received in the preceding year (§ 49). The same rules apply to 3% Defence Bonds.

Persons not ordinarily resident in the United Kingdom are exempted from tax in respect of their holdings of  $3\frac{1}{2}\%$  War Loan; 3% War Loan, 1955-59; 4% Funding Loan, 1960-90; 4% Victory Bonds; 3% Defence Bonds;  $2\frac{1}{2}\%$  National War Bonds, 1945-47;



2½% National War Bonds, 1946-48; 2½% National War Bonds, 1949-51, 2½% National War Bonds, 1951-53; 2½% National War Bonds, 1952-54; 3% Savings Bonds, 1955-65; 3% Savings Bonds, 1960-90; and 3% Savings Bonds, 1965-75 (§ 46).

The interest on National Savings Certificates is exempt from Income Tax and Sur-tax (§ 47), so long as the holder does not hold more than the maximum number of certificates authorised by the Treasury, *i.e.*, no individual may hold more than 500 full certificates and 250 of the new certificates carrying a lower yield.

#### § 4.—Schedule D.

##### (a) Income taxable under Schedule D.

Under Schedule D, tax is levied in respect of—

- (a) The annual profits or gains arising or accruing to any person residing in the United Kingdom—
  - (i) From any kind of property whatever, whether situate in the United Kingdom or elsewhere; and
  - (ii) From any trade, profession, or vocation (other than an office, employment or pension), whether carried on in the United Kingdom or elsewhere.
- (b) The annual profits or gains arising or accruing to any person whatever, whether a British subject or not, although not resident within the United Kingdom, from any property whatever in the United Kingdom, or from any trade, etc., exercised within the United Kingdom.
- (c) All interest of money, annuities and other annual profits or gains not charged by virtue of any of the other Schedules and not specially exempted from tax.

(b) The Six Cases.

The rules of assessment and charge under Sch. D are comprised in Six Cases, as follows :—

*Case I* extends to every trade carried on in the United Kingdom or elsewhere (including gasworks, waterworks, mines, etc.).

*Case II* extends to every profession and vocation carried on in the United Kingdom.

Assessments under Cases I and II are made on the basis of the profits of the trading year ending within the previous year of assessment.

*Case III* applies to profits of an uncertain annual value not chargeable under Schedule C.

The assessment is based on the full amount of the profits or gains arising within the preceding year of assessment without any deduction.

*Case IV* applies to interest arising from securities in any place outside the United Kingdom, except such as are charged under Schedule C.

*Case V* applies to income arising from stocks, shares or rents, or other possessions in any place outside the United Kingdom.

The assessment under Cases IV and V is on the same basis as Case III, except in the case of earned income and the income of persons not domiciled, and British subjects not ordinarily resident, in the United Kingdom, who are assessed on the basis of remittances to the United Kingdom in the previous year. Special rules apply to income arising in Eire (*see* Chap. X, § 16).

*Case VI* applies to annual profits or gains not falling under the other Cases of Sch. D, and not charged by virtue of any other Sch.; and the grounds on which the amount has been computed and the

average taken (if any) must be stated to the Commissioners.

The computation is made either on the actual profits for the year of assessment or according to an average of such period of not more than one year, as the Commissioners decide (§ 29—1926).

Case VI also applies to direct assessments of tax insufficiently deducted from certain interest, etc., owing to the payment having been made before the rate of tax for the year was known (§ 211) (*see* Chap. IV, § 13), and to profit rentals (*see* Chap. III, § 1 (*q*)).

The profits from letting non-rateable machinery (which is not taken into account in arriving at the Annual Value for Schedule A) are chargeable under Case VI (§ 22—1936). The profits from sub-letting furnished houses, and other isolated annual profits are also assessed under this Case.

In arriving at the profits from letting a furnished house, all expenses of obtaining the profit should be deducted from the rent received. These will include :

- (a) The proportion of rent paid or, if the house is owned, of the net annual value ; gross annual value if repairs are not charged for the period of letting.
- (b) The proportion of rates for the period.
- (c) Insurance of contents for the period.
- (d) Depreciation of furniture (commonly 5%, unless plate, cutlery and linen are included, when 10% may usually be obtained). Some districts take 10% of the gross rent where the value of the furniture is doubtful.
- (e) Cost of maintenance of garden.

- (f) Expenses of letting, advertising, agent's commission, etc.
- (g) Proportion of servant's wages, if servants are included.
- (h) Expenses of maintenance, repairs, insurance and management, unless included in a repairs claim under Schedule A.

The rent of another house occupied while the house normally occupied is let, is not deductible (*Wylie v. Eccott* (1912), 6 T.C. 128).

Where funding bonds are issued by a government, public authority, company, etc., in lieu of interest, the bonds are to be treated as income when issued, but not when redeemed. Paying agents must deduct tax, which may, where appropriate, be effected by retaining and handing to the Revenue an appropriate proportion of the bonds. If it is impracticable to deduct the tax, the owner will be assessed under Case VI. Where the bonds are quoted on the Stock Exchange, they must be valued by reference to the quotation; otherwise the value is the proceeds of sale (if sold immediately), or if not sold, a fair market value (determined on appeal where necessary) (§ 25—1938).

**(c) Mode of Assessment under Schedule D.**

Persons assessable to Income Tax under Schedule D may elect to be assessed either by the Commissioners of their district, or by the Special Commissioners.

Where the taxpayer elects to be assessed by the Special Commissioners, he must notify the Inspector of Taxes when sending in his return. This method has the advantage that the taxpayer's affairs do not come before the District Commissioners, the Collector or other local persons.

## § 5.—Schedule E.

### (a) *Incomes chargeable.*

Under Schedule E, tax is levied in respect of every office or employment of profit or pension, and upon every annuity, pension or stipend payable by the Crown or out of the public revenue of the United Kingdom, except annuities chargeable under Sch. C.

Assessments are made under this Schedule on the following, among others: All employees; Government officials; officials of the Law Courts; Army, Navy, and Air Force officers; and officers of any ecclesiastical body, public corporation, public foundation, limited company, or society.

A pension or annual payment to a former employee, or to his widow or child or a relative or dependant of his, paid by his former employer or the latter's successors, is now deemed to be income of the recipient, even if paid voluntarily and capable of being discontinued. If paid by or on behalf of a person outside the United Kingdom, it is assessable under Case V, Rule 2 (*i.e.*, on the amount *remitted* to the United Kingdom in the previous year, subject to the usual adjustments in the early and closing years). In all other cases, it is assessable under Schedule E. All such pensions, etc., are to be treated as earned income (§ 17—1932).

In practice, all pensions, the payment of which cannot be enforced at law, are chargeable under Schedule E. Those legally enforceable are treated as annual payments under Schedule D and General Rules 19 and 21, and taxed at source accordingly, unless they are paid by a business concern, in which case, if the recipient is resident in the United Kingdom,

they are allowed as expenses and assessed on the recipient under Schedule E. If the recipient is resident abroad, deduction at source is applied even when the pension is paid by a trader. (*See* § 6 (i) below regarding certain benefits.)

Any person resident in Great Britain or Northern Ireland, receiving emoluments, pension or annuity in respect of employment in the service of the Crown outside Great Britain or Northern Ireland, is assessable under Schedule E (§ 17—1923).

An actress who performs in various stage plays and acts for films and wireless, etc., does not hold anything in the nature of an office and is not assessable under Schedule E; she exercises a profession assessable under Case II, Schedule D (*Davies v. Braithwaite* (1931), 18 T.C. 198).

The “benefit” given to a professional cricketer has been held not assessable (*Reed v. Seymour* (1927), A.C. 554). The proceeds of the benefit match, both of the proportion of “gate money” and the public subscription, were considered to be a testimonial and not a perquisite; not remuneration for services, but a personal gift, expressing the gratitude of the employers and of the cricket-loving public for what the professional had already done, and their appreciation of his personal qualities.

On the other hand, a sum paid to a professional footballer “as a reward for loyal and meritorious service in lieu of presumed accrued share of benefit” on his transfer to another club, was held to be assessable (*Davis v. Harrison* (1927), 11 T.C. 707), since it arose out of an agreement under which the player served.

A non-resident director of a United Kingdom company is assessable under Sch. E on remuneration as a director (*McMillan v. Guest* (1942), T.R. 79). A taxi driver’s tips are assessable (*Calvert v. Wainwright* (1947), T.R. 1), as are all tips of hotel porters, waiters, etc.

The following receipts are not liable to tax.

- (1) Payments from the Ministry of Pensions to widows of members of His Majesty’s Forces *in respect of their children*;

- (2) Similar payments by Dominion or Colonial Governments ;
- (3) Attendant allowances to disabled officers or men given in addition to disability pensions ;
- (4) Sick-pay, strike pay, unemployment pay, victimisation benefit, funeral benefit, marriage benefit, etc., received from a trade union or friendly society.
- (5) Certain allowances, etc., of H.M. Forces (§ 30—1946).
- (6) War gratuities in connection with the war which began in 1939, to members of H.M. Forces ; Special Constables ; Police War Reserve, etc. ; N.F.S. ; Civil Defence personnel ; Coastguards ; Royal Observer Corps ; Fireguards ; N.A.A.F.I. personnel, and the Red Cross and St. John personnel, etc. (§ 23—(No. 2) 1945. Training expenses, allowances and bounties to members of reserve and auxiliary forces (§ 27—1947) ; gratuities to certain women who re-engage in women's services, etc. (§ 28—1947).
- (7) Maternity benefit and death grant under the National Insurance Act, 1946 (§ 24—1946).

Old age and widows pensions are earned income assessable on the recipient. Likewise, payments of benefit under the National Insurance Act, 1946, are earned income (§ 27 (2)—1946).

(b) *Basis of Assessment.*

The assessment is based upon the salaries, fees, etc., of the year of assessment (§ 45—1927). Members of the Forces came on to the “ actual ” basis for 1947-48 onwards (§ 30—1946).

The following classes of income have always been assessed upon the basis of the actual income for the year of assessment :—

- (a) Leave pay, pensions or annuities paid out of Government Funds of any of His Majesty's Dominions (otherwise than out of the funds of Great Britain and/or Northern Ireland) to an employee or former employee of the Crown for service outside Great Britain or Northern Ireland, or to the widow, child, relative or dependant of any such person, provided the recipient is resident in the United Kingdom (§ 17—1923 and § 45—1927).
- (b) The remuneration of any office or employment held or exercised occasionally or intermittently in the United Kingdom by a person who is not continuously resident there.
- (c) Manual weekly wage earners (§ 45—1927).  
(See Chap. III, § 6.)

For special relief given in 1939-40 to 1946-47 for diminution of earned income, see Appendix XIII.

Reference should also be made to Chap. V, § 2 (e), regarding the assessment of employments abroad.

## § 6.—Pay as you earn.

### (a) *Introduction.*

As from 6th April, 1944, the "pay as you earn" system came into operation (Income Tax (Employments) Act, 1943; Income Tax (Offices and Employments) Act, 1944; Income Tax (Employments) Regulations (S.R. & O. 1944, Nos. 251 and 1015; 1945, No. 365)). This was extended to H.M. Forces for 1947-48 onwards (§ 30—1946).



Assessment is on the actual income of the year of assessment, but tax is deducted in advance of assessment, which cannot be made until after the end of the year. The system is better described as "pay as you are paid."

The employer is made responsible for deducting from every payment of emoluments the tax appropriate to it, having regard to (a) the cumulative pay from the beginning of the year of assessment to the date of the payment in question, and (b) the proportion of the full year's allowances appropriate to the same period. The principle is that the allowances, other than the earned income allowance, are deducted weekly (or at whatever intervals the emoluments are paid). The allowances are those appropriate to the individual employee; they are ascertained and set out on a "Coding Notice" which the Inspector of Taxes sends to the employee. According to the amount of his allowances, the employee is given a Code number, which is notified to the employer on a Tax Deduction Card prepared for each employee. The allowances will be arrived at from the employee's Return of Total Income, and by supplementary information given since the Return was made.

Tax Tables have been prepared showing the tax due under each code for every amount of wages. The earned income allowance has been taken into account in preparing these tables, as has also the reduced rate relief.

Each week the employer must enter on the employee's tax deduction card the date of the pay day, the gross pay in the week, and the total gross pay from 6th April to date. From the tax tables for that week he will then find the total tax due to

date on that total gross pay and enter the amount on the card. The difference between the total tax due to date and the total deducted in previous weeks will then be deductible from the wages or repayable to the employee, and will be entered on the card in the appropriate column.

(b) *Tax Tables.*

The Tax Tables have been constructed on the basis that the employee at every stage is earning at the rate of his cumulative wages to date.

Tables are issued for weekly and for monthly cases. Where there is a large number of employees, complete tables for each week covering the usual codes will be issued, but where there are only a few employees on special codes, tables for the appropriate codes only will be issued, each covering the whole year. The tables can be seen in any office.

However much the employee's wages change, he will always be having tax deducted by reference to his yearly rate of earnings up to date, effect thereto being given by setting off the proportion of the coded allowances, and taking the earned income allowance into account in the tax. If in any week it appears that too much tax has already been deducted, the employer must refund the difference.

The employer, of course, is not directly interested in how the tables have been constructed; all he need do is to find the tax on the appropriate wages in the code applicable.

(Readers who are interested in the mathematical make-up can find it in "Pay as you earn simplified" by Jamieson & McPhie, published by MacDonald & Evans.)

(c) *Coding Notice.*

A specimen coding notice is not reproduced in this Edition ; the notice is so well known that readers can readily inspect one.

The following points should be noted in connection with the coding notice :—

(1) As the notice has to be prepared in advance of the year of assessment, it is essential that the employee shall notify the Inspector immediately his circumstances change so that he may be recoded. The employer cannot alter the tax deduction until he receives instructions from the Inspector that the employee is in another code.

(2) Earned income allowance is not included, since, as already explained, it is taken into account in the tax tables. Where, however, an employee has other sources of earned income assessable under Schedule E, the earned income allowance on that other income may be included in the coding, so that the other income is taxed at the standard rate (on a special "S.R." coding issued for it).

Similarly, where the employee's income exceeds £1,500, a restriction of earned income allowance on the excess is deducted from his allowances on his coding notice.

(3) Where the expenses, superannuation, etc., claim is material, an adjustment for earned income allowance on the expenses will be made, as this allowance can only be given on the net pay after deduction of expenses, yet the tax shown on the tables is calculated by reference to earned income allowance on the gross pay.

In some cases, the expenses allowable are such as to bring the employee's code over the maximum published. It is usual then to code him on a reduced expense allowance to bring him within the range of published codes, and to adjust by telling the employer to ignore a specified amount each week equal to the expenses omitted in the coding notice, otherwise tax is deductible from all expense allowances that are not mere reimbursement of out-of-pockets actually met.

(4) The additional personal allowance in respect of a wife's earnings is always given in her coding.

(5) Life assurance allowance, being an allowance of tax on premiums, has had to be brought into the coding by translating the allowance into terms of income. Provisional effect is given to the relief by including half the allowable premiums in the coding notice, unless the premiums amount to £100 a year or more, when only one-third of the premiums are included in the coding.

These approximations make a small difference, which is corrected in the assessment.

The contributions payable under the National Insurance Act, 1946, are allowable expenses and will be coded in accordingly.

(6) Where the taxpayer is liable only at the reduced rate, but has investment income taxed at source, effect is provisionally given for the reduced rate on the dividend income by including as an allowance in the coding a fraction of the dividends on which such relief appears to be due.

(7) Where the wife is in employment, the effect of coding both husband and wife is to give both reduced rate relief, as the allowance is given automatically

in the Tax Tables. If the over-allowance is likely to be substantial, an adjustment is made by means of a deduction from the total allowances in the coding in respect of the estimated over-allowance. A similar adjustment may be necessary where there are two or more employments, and one cannot be charged at the standard rate as in (2) above.

(8) Where other small sources of income are assessable under other Schedules, the amounts of the assessments may be deducted from the allowances in the code notice, so that all tax is deducted from pay.

(9) An adjustment (where necessary) will be made for any annual payments such as ground rent, mortgage interest, etc., from which tax is deducted, not covered by other income taxed at source; an amount being deducted from the allowances to make up the difference between standard and reduced rate.

(10) Building Society Interest payable is added to the allowances.

*(d) Tax Deduction Card.*

The Tax Card can be inspected in any office and is not reproduced here.

Tax deduction cards must be returned by the employer to the Collector at the end of the year. Where the employer prefers to keep his own records, he can omit the weekly entries on the cards, but must fill in the totals at the year end.

*(e) Payment of the tax to the Collector.*

The employer must pay over to the Collector by the 14th of each month the tax he has deducted in the previous month. Such tax is preferential in bankruptcy, winding-up, etc., for twelve months.

(f) *What constitutes pay.*

The tax deductions must be calculated by reference to the gross pay, before any deductions are made for National Insurance contributions, superannuation contributions, etc., Pay or emoluments include salary, wages, fees, overtime, bonus, commission, pension, holiday pay, payments in lieu of benefits in kind, *e.g.*, board wages, and any other emoluments assessable to Income Tax. Income from which tax cannot be deducted, *e.g.*, income in the form of shares, will be taken into account in determining the code number, and the employer will be required to make a return of these items at the end of the year.

The following items are generally not income, and should not be treated as pay :—Benefits in kind, *e.g.*, free board and lodging, or free supplies of coal ; allowances in lieu of uniform ; rent-free residence which the employee is required to occupy ; benefits under the Workmen's Compensation Acts ; payments of or contributions towards expenses that were actually incurred by the employee in connexion with the duties of his employment ; out-working or lodging allowances which are no more than reasonable payments for the extra living expenses incurred by employees employed temporarily away from home.

Tax is deductible from irregular payments in advance or on account, by reference to the Tables for the week or month in which the advance or payment on account is made. An exception arises in the case of a "sub" to a manual wage earner, which is simply a small customary payment on account of the week's wages ; in that case the gross wage (including the sub) is subject to deduction of tax when the balance is paid at the end of the week. Crediting pay to an

employee's bank account constitutes payment in the same way as payment in cash. If pay is credited in such a way that it is doubtful if it has actually been "paid," reference should be made to the tax office.

Where payments in addition to salary are made on different dates from the salary itself (*e.g.*, quarterly bonuses), tax is deductible from each additional payment by reference to the Tables for the week or month in which that payment is made. If an employee paid monthly is entitled to some relatively small additional payment (*e.g.*, for overtime, commission, bonus) besides his main monthly pay, and the additional payment is made on a different day from the main monthly payment, no tax should be deducted from the additional payment, but the amount should be included in the total pay column so that the tax will be deducted from the next payment of main pay. Tax must not be calculated on an "odd" payment when it is made, if the result would be a repayment of tax.

*(g) Refunds.*

Absence without pay will in most cases result in a repayment being due. The employee can arrange to collect it from his employer or it will be added to his next week's wages.

On becoming unemployed, a refund will usually arise, which must be applied for to the Inspector of Taxes. (*See also (v) post.*)

*(h) Change of Employer.*

On changing employers, the employee must obtain from his old employer two certificates showing the name of the employee; his number (if any), date of cessation, code number, week or month in which the

last payment of emoluments was made, cumulative emoluments, and corresponding cumulative tax. The old employer must send a similar certificate to the Inspector. The employee must hand his two certificates to the new employer, who must (*a*) insert on one copy the address of the employee, his works number (if any), and date of commencement, and send it to his Inspector; (*b*) prepare a tax deduction card in accordance with the particulars on the certificate, and (*c*) carry on deductions, as if he had employed the employee throughout the year and paid him the amount paid by the old employer. He must not, however, make any repayment on the occasion of the first payment of wages unless the refund due does not exceed £5, though he can make repayments for subsequent weeks in the normal way. In respect of the first week he must otherwise await instructions from the Inspector. An employee who objects to his new employer having details of the old employment, must deliver the two certificates to the Inspector, who will issue a new deduction card to the new employer with instructions to deduct as for the first week in the year.

Retirement on pension is not regarded as a cessation, and deduction must proceed as if the pension were pay.

The employer is responsible in the case of any employee who has no tax certificate and for whom no tax deduction card is held, for deducting tax in accordance with an emergency card, which shows the tax deductible. This, in general terms, treats the employee as single and therefore causes over-deduction pending the case being straightened out and proper instructions issued. The over-deduction will not be put right till the end of the year.



must notify the Tax Office, who will issue a Return form to the employee, preparatory to issuing a Coding Notice, etc.

*(m) Pay after leaving employer.*

If an employee receives pay from an old employer after he has left, *e.g.*, because wages are paid in arrear, the deduction of tax on such payment must be according to the Tables for the first week in the year.

*(n) Fifty-three pay days in year.*

Similarly, the first week's Tax Tables must be used for the 53rd pay day in any year. This arises where the first pay day is on 6th April and the pay day remains on the same day in every week. Leap year includes another day.

*(o) Pay at intervals other than a week.*

If wages are paid fortnightly, the Tax Tables for the 2nd, 4th, etc., weeks will be used as the pay days come round. Similarly with other intervals. Where payments are made quarterly, a full three months' tax must be deducted, although the pay days do not correspond with the quarters of the income tax year, *e.g.*, if the payments are made on 30th April, 31st July, and so on, the tax must be deducted as if the pay days were 5th July, 5th October, etc. Similarly with other regular intervals, *e.g.*, half-yearly or yearly.

*(p) Holiday pay.*

Tax on holiday pay may be paid under deduction, or the coding may be adjusted so that it can be paid gross. If, of course, holiday pay is an accumulation of weekly deductions from pay, tax will have been deducted as the pay was earned.

(q) *Gangs, etc.*

Special arrangements are made to deal with Gangs, Squads, Butty Systems, and like groups of workers.

(r) *Non-industrial workers.*

A simplified card and tax table is issued for domestic servants and similar non-industrial workers. This results in a slight over-deduction that is repaid at the end of the year.

(s) *Modified scheme.*

Any employer, with the agreement of his workers and the Inspector, may adopt a modified scheme, whereby he uses the simplified table for three weeks and adjusts to the correct tables on the fourth, or more frequently. It is not allowed to adjust less frequently than each fourth week. This has the benefit of allowing the work of preparing the wage records to be spread over the week, except in the adjustment weeks. It involves a small over-deduction in the intermediate weeks, and delays repayments, where applicable, until the adjustment week. The special cards required must be provided at the employers' expense.

(t) *Audit.*

The Revenue have officers who are empowered to call on any employer and conduct an audit of the pay and tax deduction records. Income Tax (Employments) Officers will also be pleased to call at factories, etc., to settle wage-earners' difficulties, and at all times to assist employers and employees.

(u) *Casual Employees.*

Where a casual employee is engaged for a period of less than one week, the employer need not deduct

tax unless the actual earnings of the employee exceed £2 5s. or, £1 if the employee is known to have other employment. If the period of employment is one week or more, and no form from the previous employer is produced, the employer must at once notify the Inspector, and deduct on the emergency card until instructions are received.

*(v) Employees becoming unemployed.*

By arrangement between the Inland Revenue and the Ministry of Labour and National Service, unemployed taxpayers who are paid benefit or allowances in cash by local offices of the Ministry or by postal draft, will receive their income tax repayments under P.A.Y.E. along with their weekly payments of benefit or allowances. This arrangement also applies to most cases where benefit or allowances are paid through associations to members. It does not cover juveniles (under 18), persons whose allowances are paid by Area Offices of the Assistance Board, or persons who receive benefit under the special scheme for banking and insurance industries. The Revenue certify to the Employment Exchange the weekly repayment. To obtain the first repayment, the wage-earner has to complete a simple form, of which employers hold a stock. Where these arrangements are unsuitable, the Revenue repay direct.

**§ 7.—Miscellaneous Schedule E matters.**

*(a) Application of Income.*

The application of income does not affect the liability to tax thereon, *e.g.*, where a director applied undrawn fees and commission to paying up new shares (which were of doubtful value), he was held to be assessable upon the full amount of remuneration

credited to him (*Parker v. Chapman* (1927), 13 T.C. 677).

(b) *Return of Expenses, etc.*

The employer must enter on the appropriate section of the Tax Deduction Card all "round sum" payments for expenses in excess of £25 for the year. This arises from the provision that an employer is liable to show—

- (a) any payments to employed persons in respect of expenses ;
- (b) any payments made on behalf of employed persons and not repaid ; and
- (c) any payments made to the employees in the trade or business for services rendered in connection with the trade or business, whether the services were rendered in the course of their employment or not (§ 19 (1)—1939).

The above provisions prevent the evasion of tax by what had become a common device of making "expense allowances" out of all proportion to the disbursements of the employees.

These additional particulars are dealt with in a reasonable way, and there need *not* be included—

- (i) Payments in respect of expenses which represent no more than the recoupment of, or provision for, expenses that were actually incurred by the employee in the performance of the duties of his employment ; or
- (ii) Payments for expenses made in accordance with a regular scale, provided that the employer will furnish to the Inspector of Taxes particulars of the scale and such other information as he may require as to the amounts paid in a specified case.

Where, in the course of the trade or business, or in connection with its formation, acquisition, development or disposal, an individual who is not an employee of the person carrying on the business, has been paid, or has received other consideration as a commission for services rendered, the Inspector of Taxes may require the person carrying on the business to make a return showing—

- (a) The names and addresses of the individuals to whom the payments were made or consideration given ;
- (b) The amount of the payment or particulars of the consideration, as the case may be.

Particulars need not be given in any case where the payments to an individual in the year covered by the return do not exceed £15 (§ 19 (2)—1939).

(c) *Tax free remuneration.*

Where a salary is paid “ free of Income Tax ” (*i.e.*, the employer pays the tax for the employee), the Schedule E assessment should be computed by reference to the amount of salary actually paid plus the tax thereon borne by the employer (*North British Rly. Co. v. Scott* (1923), A.C. 37), even where the payment of tax is voluntary on the part of the employer (*Hartland v. Diggines*, (1926), A.C. 289). This question is discussed more fully in Chap. XI, § 8.

The employer must calculate the gross pay and appropriate tax for insertion on the tax deduction card.

(d) *Expenses and deductions allowable.*

Where a person assessable under Schedule E is obliged to incur and defray out of his emoluments travelling or any other EXPENSES WHICH ARE WHOLLY,

EXCLUSIVELY AND NECESSARILY DISBURSED IN THE PERFORMANCE OF THE DUTIES of his office, he is permitted to deduct such expenses from the amount of his emoluments from that office (Sch. E, R. 9). As already stated, a provisional allowance will be given in the coding notice, to be adjusted in the assessment. No deduction is permissible for travelling expenses of employees from their residences to the premises of the employer, since the duties do not commence until the employee reaches the place of employment. If an employee holds an office in one town and a separate employment in another town, the expenses of travelling between the two towns are not allowed, since each employment commences when the employee reaches the place of employment (*Ricketts v. Colquhoun* (1926), A.C. 1). But if a person's place of work or residence has changed through circumstances connected with the war, and in consequence he has to incur or defray out of his emoluments of the employment additional expense in travelling between his residence and his work, he can claim a deduction of such additional expenditure, not exceeding £10 in any year (§ 23—1941 ; § 26—1942).

Even where, owing to a housing shortage, an employee has to live at a distance from his work, his travelling expenses, not being incurred in the performance of his duties, are not a permissible deduction (*Andrews v. Astley* (1924), 8 T.C. 589).

A schoolmaster is not entitled to deduct the cost of a domestic servant employed to carry on the duties of his household, while his wife (a mistress in the same school at a joint salary) is engaged at the school, the expenses not being incurred in the performance of the duties of the offices of master and mistress of the school (*Bowers v. Harding* (1891), 3 T.C. 22).

Voluntary contributions by a minister towards his assistant's stipend are not expenses, wholly, exclusively and necessarily

incurred in the performance of his duty (*Lothian v. Macrae* (1884), 2 T.C. 65). Nor is the expenditure incurred in obtaining an augmentation of stipend or a pulpit supply during holidays allowable as an expense (*Jardine v. Gillespie* (1906), 5 T.C. 263).

Subscriptions to professional societies, where membership of those societies is not a condition of the employment, are not expenses wholly, exclusively and necessarily incurred in the performance of the duties of the office (*Simpson v. Tate* (1925), 9 T.C. 314). If, however, membership of the professional society is a condition of employment, the subscription is usually allowed as a deduction; though not as of right (*Wales v. Graham* (1941), T.R. 217).

The following are allowable deductions from the amount of the emoluments :—

Contributions under the National Insurance Act, 1946.

Annual contributions paid to a superannuation fund approved by the Commissioners of Inland Revenue under the provisions of the Income Tax Acts (§ 32—1921).

Contributions made under the requirements of any public general Act of Parliament towards the expenses of providing a superannuation allowance or gratuity on retirement or death, *e.g.*, contributions required under the Teachers' (Superannuation) Acts, 1918 to 1925, the Police Pensions Act, 1921, etc. The name of the fund or Act should be quoted in the return.

In the case of a clergyman or minister who uses any part of his dwelling-house mainly and substantially for the purposes of his duty, a corresponding part of the rent or annual value of the house, not exceeding one-fourth (one-eighth prior to 1944-45) (Gen. R. 2, § 22—1944). If, however, the minister is bound to live in the manse provided and the congregation pay the rates and tax, the tax under Sch. A is not part of his income, but he is not entitled to the deduction under Gen. R. 2 as he is not the "occupier" for tax purposes (*C.I.R. v. Leckie* (1940), T.R. 211).

Where any plant or machinery (*e.g.*, a motor car) is used for the purpose of earning the emoluments, and the expenditure is wholly, exclusively and

necessarily incurred, initial and wear and tear allowances can be claimed as well as running expenses. In such cases, the car or other machine may be used partly for private purposes, and only a due proportion of the expenses, etc., can then be claimed as a deduction. The amount is usually agreed with the Inspector of Taxes on a mileage or similar basis, or may be decided on appeal by the Commissioners. The calculation of these allowances is explained in Chap. IV, § 3. The cost of replacement of utensils may be allowed as an alternative to wear and tear and obsolescence allowances.

In the case of manual wage earners, expenses include special tools, boots, overalls, explosives, etc. The trade union agrees a scale for the particular trade with the Board of Inland Revenue; in cases where there is no trade union, the allowance is agreed with the Inspector or fixed by the Commissioners on appeal.

*(e) Compensation or Lump Sum Payments.*

A gift by an employer to an employee on the conclusion of 25 years service, whether in cash or savings certificates, is a gratuity by way of bonus, and assessable on the recipient. An employer cannot relieve his employee from his obligation to pay income tax by saying he does not intend it as remuneration (*Western v. Hearn*; *Carmouche v. Hearn* (1943), T.R. 295).

A sum of money paid to an employee as compensation for loss of office, *e.g.*, on liquidation, and not in respect of services rendered, is not assessable on the recipient (*Chibbett v. Robinson & Sons* (1924), 9 T.C. 48), although it may be an allowable deduction in the Profit and Loss Account of the payer (*Mitchell v. Noble* (1927), 11 T.C. 372). If the liquidator makes



a payment to an officer of the company "for services rendered" prior to liquidation, the payment is taxable on the recipient (*Shipway v. Skidmore* (1932), 16 T.C. 748). A payment to make up for the cessation for the future of annual taxable profits is not itself an annual profit at all (*Chibbett v. Robinson & Sons, supra*).

Where, however, there is a direct relation between the holding of the office and the right to the payment of the compensation, so that the payer is under a contract to make the payment, which could be enforced by action, and the recipient took office on the terms that on retirement he would be entitled to such compensation, the recipient is liable to tax thereon as remuneration (*Henry v. Foster* (1932), 16 T.C. 605). On the other hand, where there is a contract under the Articles to pay such compensation, and the company pays a lump sum to vary such contract (i.e., to obtain a release from a contingent liability), this sum is a capital payment not assessable on the recipient (*Hunter v. Dewhurst* (1932), 16 T.C. 605). Compensation for giving up a right to remuneration is not taxable (*Duff v. Barlow* (1941), T.R. 17), nor is the capitalisation of a pension, but the consideration for agreeing to serve at a smaller salary arises from the office and is assessable (*Wales v. Tilly* (1943), T.R. 45). (See below, however, in connection with certain benefits.)

A payment by way of deferred remuneration is taxable; the fact that it falls to be paid after the office has come to an end does not divorce it from the office, but there must be a direct relation between the holding of the office and the right to have the payment made (*Hunter v. Dewhurst* (1932), 16 T.C. 629, 630). Thus a payment to the executors of a

deceased employee under a service agreement whereby upon the final termination from any cause (other than wilful misconduct) of the service a sum of money is payable to the employee, is assessable on the executors under Sch. E as if it had been received by the deceased while alive (*Allen v. Trehearne* (1938), 2 K.B. 464). Wages paid in lieu of notice are not assessable.

Where a company paid a large sum of money to a director in consideration of his refraining from carrying out his intention of resigning his office, the Court considered that the true consideration was the desire of the company that he should continue as a director and the payment arose from his office as director and was properly assessed under Schedule E (*Prendergast v. Cameron* (1940), T.R. 163). A payment in connection with giving up a right wholly unconnected with the office, *e.g.*, a restrictive covenant operative only when the office is no longer held, is not income (*Beak v. Robson* (1942), T.R. 95).

A lump sum payment to a person in complete control of a company by way of compensation for loss of office and the cessation of remuneration was held to be remuneration in the hands of the recipient; in view of the commanding position he held in the company, he could not be said to have been "deprived" of his office (*Wilson v. Daniels* (1943), T.R. 345). The lump sum was allowed as a proper deduction in computing the company's profits (*Wilson v. Nicholson & Sons and Daniels* (1943), T.R. 345).

Where a director waived his director's fees but continued his duties, he did not thereby cease to hold an "office of profit." Accordingly, he was assessable for that year in the usual way, *i.e.*, on the fees for the

previous year (*Oliver v. Chuter* (1934), 18 T.C. 570), but see Appendix XIII for relief for diminution of income owing to the war.

(f) *Retirement and other benefits* (§§ 19–23—1947).

Complicated provisions designed to prevent avoidance of the tax are enacted in the 1947 Act. These are reproduced in Appendix XIV. They deal with various schemes under which a company has paid sums year by year to insurance companies or trustees to provide retirement or other benefits for directors or employees, and with conditions of service under which a company has undertaken to provide such benefits.

Where the benefits consist of non-taxable lump sums or of annuities or pensions convertible into non-taxable lump sums, or are wholly disproportionate and in excess of what might be described as a reasonable pension, the amount paid by the employer is to be treated as income of the employee, assessable under Schedule E. If no amount is paid by the company year by year to secure the benefit, and the benefit is to be provided out of the funds of the company, a notional figure will be attributed to the employee as taxable income during each year of his employment. The notional figure is the amount that would have to be paid to a third party to provide the benefit. The following will be excepted: (a) statutory superannuation schemes; (b) schemes approved under Section 32, Finance Act, 1921; and (c) schemes approved under the new clauses. Under (c) the Commissioners are to approve certain schemes where the amount is paid by the company for an annuity and certain requirements are satisfied; broadly speaking, this means that they will approve a *bona fide* super-

annuation scheme. Where the employee is charged to tax in respect of an assurance premium, he will get life assurance relief on it under the usual rules.

Service while a controlling director is not to be taken into account in an approved scheme.

Any scheme existing before 6th April, 1944, where the main benefit to be provided is a life pension or annuity, is exempted.

Small provident funds and endowment insurance schemes providing for small lump sum payments are also exempted. The limit is that the employer must not pay more than 10 per cent. of the employee's remuneration to the fund or more than £100, whichever is less ; the employee's salary must not exceed £2,000.

If an employee is dismissed or can show that he will not get the benefit, he can reclaim tax.

Employees abroad not assessable under Schedule E are left out of the new imposition.

Existing schemes can be amended and, if approved, the approval dated back to April, 1947. The change must be made by April, 1948, but the Commissioners may extend the time.

*(g) Rent-free Residence, etc.*

In some cases, an employee is allowed or required to live on the premises where the business is carried on (*e.g.*, a bank manager), or is provided, rent free, with a dwelling house as part of his remuneration (*e.g.*, estate employees). In such cases the employers have the use of the premises, and are therefore the legal occupiers, assessable under Schedule A. Although the employee resides in the premises he does so as the servant of his employer, and for the purpose of performing the duty he owes to his employer, and the tax is no more leviable on him than it would be on a

caretaker, nor can assessments be made on him under any other Schedule in respect of the premises (*Tennant v. Smith* (1892), 3 T.C. 158). Whether the employee has power to let or turn his benefit into cash is not relevant (*C.I.R. v. Miller* (1930), A.C. 222; *Reed v. Cattermole* (1936), 21 T.C. 35), except as a factor helping to show the true position.

If, however, the house is not provided for the purpose of enabling the duties to be performed, but is provided as a reward in the performance of the employer's contract to pay the employee, and as a convenience for the employee, who may live there or not as he pleases, the employee would normally be the legal occupier. In other words, the question turns on "whether it is a right or a duty" of the employee to live in the house. A legal right to occupy would make it income of the employee; a duty implies permission to make use of the house, which is therefore the income of the person permitting the user, viz., the employer.

If the employee is the occupier within the meaning of the Rules of Schedule A, he is assessable under that Schedule, and if he has no recourse to any other person for the tax, because he pays no rent, the annual value is part of his income. If the employer can be regarded as the legal occupier, then the employee's income cannot include the annual value.

Where an employee is provided with board and lodging or some similar advantage, the value of this perquisite cannot be added to the wages for the purposes of taxation unless the advantage can be turned into money (*Machon v. McLoughlin* (1926), 11 T.C. at p. 89). If, however, the charge for board, etc., is deducted from the remuneration, the employee

is chargeable to tax on the gross remuneration (*Cordy v. Gordon* (1925), 9 T.C. 304; *Machon v. McLoughlin* (1926), 11 T.C. 83).

Where it is the custom of an employer to make gifts in kind to employees at Christmas, and owing to goods being unobtainable, National Savings Certificates are given, the Revenue do not seek to assess the value of the gifts. Such Certificates given as a bonus or as additional remuneration, however, are taxable.

(h) *Error or Mistake.*

The provisions of § 24, 1923, which provide for relief in respect of error or mistake, apply to tax charged under an assessment under Schedule E as they apply to tax charged under an assessment made under Schedule D (§ 45 (8)—1927). (*See* Chap. II, § 31.)

Appeal against an assessment under Schedule E can, if desired by the taxpayer, be made to the Special Commissioners (§ 19—1922), or to the General Commissioners (§ 136).

(i) *Commission on Net Profits.*

Since Income Tax is an appropriation of profits (*Ashton Gas Co. v. Attorney-General* (1906), A.C. 10), Income Tax is not deductible from profits in arriving at a commission on "net profits" payable under an agreement with a manager (*Johnston v. Chestergate Hat Manufacturing Co.* (1915), 2 Ch. 338).

## § 8.—Discharge of Income Tax for 1943-44.

(a) *General Rules.*

The introduction of "pay as you earn" would have placed an intolerable burden on Schedule E taxpayers if they had had to pay up the tax still due for 1943-44 while having tax for 1944-45 deducted from current

earnings. Discharge of the overhanging tax, while not a desirable thing in itself, was felt to be the only practical solution. Accordingly, there was discharged—

- (a) Ten-twelfths of the manual weekly wage-earners' tax for 1943-44 (*i.e.*, the tax deductible from April, 1944, to January, 1945).
- (b) Seven-twelfths of all other Schedule E tax for 1943-44 which was collectible in the ordinary way (*i.e.*, that due for collection April—October, 1944); and
- (c) The overhanging portion of tax due for collection after 5th April, 1944, in respect of 1943-44, in those cases (such as railway employees) where some other method of deduction was in force.

In these cases, the amount of the discharge was calculated on the assumption that all allowances were given against earned income, but, except that earned income allowance was applied to its appropriate source (if the maximum of £150 applied, this was given proportionately on all earned income), and the additional personal allowance was always set against the wife's earned income, the allowances were to be applied in the manner most advantageous to the taxpayer, so as to give him the maximum discharge.

**Example.**—Taxpayer with three sources—

		Sch. D, Case I.	Sch. E, Directors' Fees.	Manual Wage Earner.
		£	£	£
Assessment 1943-44	..	200	100	316
E.I.R.	.. ..	£20	£10	£32
P.A.	.. ..	140	—	—
Ch.A.	.. ..	40	60	—
		200	70	32
		<u>nil</u>	<u>£30</u>	<u>£284</u>

	Fees.		Wages.
£30 at 6/6 =	£9 15 0	£135 at 6/6 =	£43 17 6
		149 at 10/- =	74 10 0
			<u>£118 7 6</u>
Discharge .. 7/12ths.	<u>£5 13 9</u>	10/12ths.	<u>£98 12 11</u>

To avoid issuing new deduction notices for the period beginning 1st February, 1944, the Revenue instructed employers to continue deduction from employees' pay for the period 1st February—5th April, 1944, of one-third of the tax which was deductible for the preceding half-year to 31st January, 1944.

The Post War Credit for 1943-44 is reduced (in most cases extinguished) by the deduction from it of the tax discharged.

In order to qualify for discharge, the employee must have been entitled to emoluments at some time during 1944-45. If therefore he retired without pension, or died, prior to 6th April, 1944, he had no discharge. If the cessation occurs, otherwise than through death or unemployment, after 5th April, 1944, the discharge will only operate for the period after 5th April, 1944, that he was entitled to emoluments.

Tax found to be overpaid was either repaid (on a claim being made) or coded into 1945-46. Underpayments were coded into 1945-46, and where necessary, later years.

(b) *Armed Forces.*

These continued under Schedule E old assessment rules until 5th April, 1947. Tax has always been deducted over the year ended 5th April, but this is not strictly "pay as you earn," owing to the assessment being based on the preceding year's pay. A



valuable privilege for 1944-45 to 1946-47 was, however, given, of having the assessment of any year reduced to the actual emoluments of that year.

*(c) Crown or Railway Employees.*

In the case of a person in Crown or railway employment (*i.e.*, falling under Rule 7 or 11 of Schedule E), on 6th April, 1944, who still owed Income Tax for a year before 1943-44 in respect of an employment held before he entered Crown or railway employment, and the tax so outstanding was due for payment not earlier than the date he entered the Crown or railway employment, that tax is to be discharged.

A railway employee, whose tax for 1943-44 was ordinarily collected by deduction, over a period part of which overlapped into 1943-44, for the purposes of the above is regarded as having entered that employment on a date later than the actual date by a period equal to the period of the overlap.

Tax under the above rule will not be discharged if, under arrangements in operation on 1st February, 1944, it was to be collected before 6th April, 1944.

A person who was before 6th April, 1944, in Crown or railway employment, but was not in such employment on that date, is entitled to the discharge only if, since the cessation of such employment, he has died or been continuously unemployed.

*(d) Increases in Remuneration in 1943-44.*

In order to prevent avoidance of tax in 1943-44 by unusual increases in pay then assessable on the previous year basis, an additional assessment may be made for 1943-44 on additional remuneration granted after 20th September, 1943, or on any increase by

reason of a change in the conditions of service, effected after that date. The additional tax will not rank for discharge; sur-tax will be payable where relevant on the additional assessment.

These penal provisions do not apply to promotion in the ordinary course of events, ordinary application of an incremental scale of emoluments, or overtime paid at ordinary rates, or similar increases of an ordinary character.

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## CHAPTER IV.

## SCHEDULE D.

## CASES I AND II.

**§ 1.—Basis of Assessment under Schedule D.**

With the exception of Case VI, the basis of assessment under Schedule D is the income of the year preceding the year of assessment, *i.e.*, the “previous year’s” income. By the previous year is meant the preceding Income Tax year, unless the Acts lay down some other period. In Cases I and II such other period *is* laid down, *viz.*, the accounting period of the business ended in such previous year. The rules for determining the accounting period are explained in Chap. IV, § 7.

Special rules are provided for the basis of assessment where a preceding year is not available, *e.g.*, in the early years of a business, or of the holding of a source of income. These are explained hereafter as they arise.

**§ 2.—Rules and Regulations for Calculating Profits.**

The profit shown by the accounts of a business will not usually represent the profit for Income Tax purposes, quite apart from the assessment being based on the profits of the previous year. As the accounts are prepared on commercial principles, adjustments are commonly necessary in order to arrive at the profit in accordance with the Income Tax Acts. The adjustments will comprise :—

- (a) Adding to the net profit shown by the accounts, any expenses which have been debited before

arriving at the net profit, but which the Acts do not permit as deductions for Income Tax purposes ;

- (b) Deducting any items which have been credited in arriving at the profits, but which are not required to be included in the profit for Income Tax purposes ;
- (c) Deducting any expense which has not been charged in the accounts, but which the Acts allow to be deducted ;
- (d) Adding any trading income which has not been credited in the accounts.

These will mainly fall under certain classes as follows :—

(a) *Expenses disallowed*—

- (1) Expenditure or losses of a CAPITAL nature which may have been charged to revenue, such as improvements to premises, extension of plant, depreciation (although an allowance may be claimed in the assessment in respect of industrial buildings and plant and machinery as explained later). Although it may be prudent for the taxpayer to charge such items to his Profit and Loss Account, the Income Tax Acts do not recognise such losses as expenses in arriving at the income to be taxed.
- (2) APPROPRIATIONS OF PROFIT, such as Income Tax (which being a levy on the profits is legally an appropriation of profit and not a charge) ; all general reserves, whether made against anticipated losses or not ; voluntary gifts\*, etc. ;

\* But gifts in kind, e.g., at Christmas, to employees (including National Savings Certificates given in lieu owing to goods being unobtainable) are allowed, as are so-called gifts that are in fact emoluments of the recipient's office.

dividends and similar distributions of profit, and adjustments between the proprietors of the business, *e.g.*, partners' salaries, interest on capital, and similar items, which are merely charged in the Profit and Loss Account for the purpose of adjusting the rights of the partners as between themselves.

- (3) PAYMENTS TAXABLE AT THE SOURCE, such as annual interest on loans, annuities, royalties on patents, etc. The payer of the annual interest, etc., is entitled to recoup himself by deducting Income Tax from the interest which he pays, and cannot be allowed to reduce his income by the interest as well, otherwise he would not account to the Revenue for the tax deducted.
- (4) LOSSES NOT CONNECTED WITH OR ARISING OUT OF THE TRADE.
- (5) EXPENSES NOT WHOLLY AND EXCLUSIVELY LAID OUT FOR THE PURPOSE OF EARNING THE PROFITS.

(b) *Receipts which can be excluded---*

- (1) Capital profits and receipts.
- (2) Transfers from general reserves which were disallowed when set aside, and therefore already charged to tax.
- (3) Income received less tax.
- (4) Profits not connected with or arising out of the trade. If chargeable to tax, such profits must be assessed under the appropriate case or schedule, and not as part of the profits from the trade. (A dividend from a co-operative society in proportion to purchases must be included in a trader's profit and loss account (*Pope v. Beaumont* (1941), T.R. 151)).

(5) ANY OTHER INCOME WHICH IS ASSESSABLE  
UNDER SOME OTHER CASE OR SCHEDULE.

(c) *Allowable expenses which have not been charged in  
the accounts—*

Care must be taken, to adjust for these items, which commonly arise where a residence is partly used for business purposes, as in the case of a doctor.

The following are lists of items which commonly require adjustment (Sch. D, Cases I and II, R. 3); these are explained more fully in later pages.

(a) **Deductions are allowed for—**

(i) Repairs of premises occupied for the purpose of the trade, etc., and for the supply or repair of implements, utensils, or articles employed. Any element of improvement will be disallowed.

(ii) Debts proved to be bad; also for doubtful debts to the extent that they are respectively estimated to be bad (*i.e.*, a reserve against specific debts is allowed, but a reserve against debtors generally, *e.g.*, one based on a percentage of debtors, is not).

(iii) The rent of business premises or alternatively (if the premises are within Great Britain or Northern Ireland) the net annual value, whichever is higher. If part of the premises is used as a residence, only the appropriate proportion of the rent or net annual value is allowable.

Where lands are occupied for the purpose of the trade and separately assessed under Sch. B or Sch. D, it is the practice to allow the Sch. B or D assessment as a deduction, as otherwise double assessment would arise. Usually, however, the separate assessment will be discharged, and no deduction from profits allowed for the purpose of Sch. D.

(iv) The amount charged to United Kingdom tax on account of premises situate in Eire to the extent that they are used for the purposes of the trade.

(v) The Profits Tax or the Excess Profits Tax charged on the profits of the period covered by the accounts. Excess Profits Tax recovered on deficiencies must be left in charge to Income Tax in the year in which the deficiency occurs, unless it has been deducted from unpaid E.P.T. of a previous year, when only the net E.P.T. for that earlier year would be allowed in the year for which it was paid.

(vi) Insurance premiums on policies of indemnity in respect of the business, *e.g.*, fire, burglary, workmen's compensation, employers' liability, loss of profits, etc.; insurance of goods, etc., under the War Risks Insurance Act, 1939, marine or aircraft insurance, or goods in transit (§ 12—(No. 2) 1940).

(vii) Any ordinary annual contribution to an approved superannuation fund.

(viii) Contributions in furtherance of approved schemes for the rationalisation of industry.

(ix) Any other disbursements or expenses wholly and exclusively laid out for the purposes of the trade, etc.

(x) Expenditure on repairs, etc., making good war damage only in so far as the taxpayer is *not* entitled to a payment in respect of the damage (§ 113, War Damage Act, 1943).

**(b) Deductions are not allowed for—**

(i) Sums not wholly and exclusively incurred for the purposes of the trade, etc.

(ii) Annual interest, annuity, or other annual payment, payable out of the profits or gains, or for any

royalty or other sum paid in respect of the user of a patent.

The prohibition is treated as extending to interest under a foreign as well as under a British mortgage. There is one exception to this, however, *viz.*, where a trader, resident in the United Kingdom, has purchased trade premises abroad and the premises were at the time of purchase mortgaged. In such a case the mortgage interest is allowed as a deduction in computing the profits of the trade, the justification for the allowance being that only the equity of redemption had been acquired as an asset of the trade (Report I.T.C.C.).

(iii) Sums charged as salaries to sole traders or partners, or any interest on capital, or drawings by such persons.

(iv) Sums invested or employed as capital in the trade, etc., or any capital withdrawn therefrom.

(v) Sums expended in improvement of premises, or written off for depreciation of land, buildings or leases.

(vi) Losses not connected with, or arising out of the trade, etc.

(vii) Expenses of maintenance of the persons assessable, their families, or establishments; or for any sum expended for any other domestic or private purpose.

(viii) Losses recoverable under an insurance or contract of indemnity. Where stock has been destroyed by fire, the full amount recovered in respect thereof under an insurance policy is a trading receipt and must be credited in computing the profits for Income Tax purposes (*Green v. Gliksten* (1929), A.C. 381). Recoveries under loss of profits policies are also assessable (practice of Inland Revenue following the decision of the Privy Council in *The King v. British Columbia Fir and Cedar Lumber Co.* (1932), A.C. 441).



So are compensations received by a company under an employers' liability policy (the premiums being allowed as deductions as paid) (*Murphy v. Thos. E. Gray & Co.* (1940), T.R. 275), and the proceeds of a policy of insurance against death or disablement of a director (*C.I.R. v. Williams' Exors.* (1944), T.R. 33).

(ix) United Kingdom Income Tax, and any sum paid as Dominion Income Tax except in certain circumstances (*see* Chap. X, § 15). Foreign Income Tax paid in respect of the profits in the place where they arise may, however, be deducted, unless there is an arrangement between this country and the country where the income arises for double taxation relief (*see* Chap. X). No deduction can be made for interest on arrears of Income Tax, Sur-Tax, E.P.T. or Profits Tax (§ 8—(No. 2) 1947).

(x) Wear and tear of machinery and plant; but an allowance may be claimed in the assessment in respect of this item and of capital expenditure on industrial buildings, and for exceptional depreciation owing to the war, of buildings and plant in certain cases (*see* Chap. IV, § 3).

(xi) The rent or net annual value of any dwelling-house or domestic offices or any part thereof, except such part as is used for the purposes of the trade or profession.

(xii) Contributions under Parts I and II of the War Damage Act, 1943 (§ 113 *ibid.*) or payments into mutual pools for meeting war damage (§ 12—(No. 2) 1940).

(xiii) Payments by way of benefit to any employee or to his personal representatives or dependants, on account of his incapacity, retirement or death owing to war injuries, and any premium or contribution under any policy, agreement, scheme or arrangement providing for such payments (§ 17—1941).

The prohibition does not apply, however—

- (a) To a payment payable under a policy, agreement, etc., made before 3rd September, 1939, except to the extent of any increase as a result of a variation of the policy, etc., made on or after that date; or
- (b) If the Commissioners of Inland Revenue consider that the payment of a benefit is made under an established practice which is such that the same or a greater payment would be made if the disability or death had not been due to war injuries.

Moreover, if the Commissioners are satisfied that there is an established practice under which a smaller payment of benefit would have been made if war injuries had not been the cause of the disability, etc., they may allow that smaller amount. Payments under a policy, etc., are to be apportioned to exclude the premium for war risk, where appropriate.

(xiv) Any expenditure on repairing or otherwise making good war damage in so far as the persons assessable are entitled to reimbursement under the War Damage Act, 1943.

**(c) Decisions as to Items allowed or not allowed.**

The fact that expenditure is necessary to enable profits to be earned is inconclusive as regards its admissibility as a deduction, *e.g.*, it may be capital expenditure (*Ounsworth v. Vickers* (1915), 6 T.C. at p. 677). Many cases are fought in the Courts as to what expenses are proper deductions.

The following are some of the more important decisions :—

**(i) Deductions allowed—**

- (a) A payment for services rendered to the business, even if the remuneration is calculated as a percentage of net profits (*British Sugar Manufacturers v. Harris* (1938), 1 A.E.R. 149).

- (b) A payment of £500 per annum for the goodwill of a cinema business. In this case the company acquired an under-lease of premises used as a cinema at an annual rent. At the same time it acquired for the period of the under-lease the goodwill of the cinema business there carried on subject to a payment of £500 per annum, with an option to purchase the head-lease and goodwill for £3,500. It was held that the £500 was a revenue expense, chargeable against the profits of the company. It was not a capital payment, nor was it an annual payment from which tax was deductible; it was a revenue payment for the use of certain valuable rights (*Ogden v. Medway Cinemas* (1934), 18 T.C. 691).
- (c) Bad Debts in respect of cash advances made for the purposes of the trade (*Reid's Brewery Co. v. Male* (1891), 2 Q.B.1).
- (d) A lump sum payment to discharge an onerous contract, thereby relieving future revenue without acquiring any new asset or enhancing the value of existing capital (*Anglo-Persian Oil Co. v. Dale* (1931), 16 T.C. 253).
- (e) A lump sum payment to a director (who has been appointed for life) to secure his retirement (*Mitchell v. Noble* (1927), 11 T.C. 372). A payment to get rid of a servant in the interests of the trade is a proper deduction (*ibid.* 415).
- (f) Expenditure of a rubber company for superintendence, weeding, etc., on the whole estate, although only one-seventh produced rubber (the remainder being in process of cultivation for production of rubber) (*Vallambrosa Rubber Co. v. Farmer* (1910), 5 T.C. 529).
- (g) A payment to protect title to land abroad, used for the purposes of the business (*Southern v. Borax Consolidated* (1940), T.R. 475).
- (h) Payments properly made by a company for the compromise of an action (*Scammell & Nephew v. Rowles* (1939), 1 A.E.R. 337).
- (i) Moneys expended to meet a guarantee of a bank overdraft advanced to a company formed to produce a picture (which proved a failure), and loans by the producer for the same purpose. "He was to produce a film which the trade would consider showed that he was a talented, artistic producer of films, so that the trade, impressed

with his merits as an artistic producer, would be disposed to employ him. The money was expended to gain the the good opinion of the trade. To describe it as capital in the business of an artistic film product seems to me to be a misuse of language..." (*Macnaughten, J.*) (*Lunt v. Wellesley* (1945), T.R. 309).

(ii) Deductions not allowed.—

- (a) Interest on a loan raised for the purpose of providing capital to be used in a company's business is a capital expense (*Ward v. Anglo-American Oil Co.* (1934), 19 T.C. 94). (Annual interest is disallowable in any event; but even "short" interest from which Income Tax is not deductible at source may be disallowable because it is for "capital" purposes. It seems that bank interest would not be caught in the "capital" net in view of the peremptory terms of § 36—1918.)
- (b) Debenture interest paid by an English company to foreign debenture-holders, in respect of debentures charged on foreign property (*Alexandria Water Co. v. Musgrave* (1883), 11 Q.B.D. 174).
- (c) Expense of issuing debentures (*Texas Land & Mortgage Co. v. Holtham* (1894), 10 T.L.R. 337).
- (d) Owner's Rates (Scotland) are not an admissible deduction in computing profits under Schedule D (*C.I.R. v. Scottish Central Electric Power Company* (1931), 15 T.C. 761). These rates are an admissible deduction in arriving at the Net Annual Value under Schedule A (No. V, R. 4 (1)). (Some authorities doubt whether this decision is now applicable since the amendment in the method of giving relief for depreciation of mills, factories, etc., by § 15—1937.)
- (e) Bonus payable on repayment of borrowed money (*Arizona Copper Co. v. Smiles* (1891), 29 Sc. L.R. 134).
- (f) Loss incurred through closing a factory, and removing and reopening elsewhere on a smaller scale; the loss is a loss of capital (*Smith v. Westinghouse Brake Co.* (1888), 2 T.C. 357).
- (g) Legal costs in connection with an appeal to the Commissioners (*Allen v. Farquharson Bros. & Co.* (1932), 17 T.C. 59; *Rushden Heel Co. v. C.I.R.* (1947), T.R. 165; *Smith's Potato Estates v. Bolland* (1947), T.R. 171), but by

concession, the costs of a successful appeal against a sur-tax assessment on a company under § 21, 1922, are allowed. The costs are paid in the capacity of taxpayer and not as a business expense.

- (h) The loss arising to a company where, on the death of its managing director, it was found that payments, etc., relating to his private affairs had passed through the books; the loss was not a trading loss (*Curtis v. Oldfield* (1925), 9 T.C. 319).

(It should be noted that by virtue of his position as managing director, he could do exactly what he liked. Defalcations by subordinate employees are allowed as deductions except to the extent that they are recovered from the delinquent or under an insurance policy.)

- (i) Deduction in respect of exhaustion of nitrate deposits, in the case of a company owning grounds situate abroad on which is found the raw material from which the nitrate is produced (*Alianza Co. v. Bell* (1906), A.C. 18).

On the other hand, where a company acquired from another company their rights in certain dumps of "tailings" or residuals from gold mines, the purchase price of the tailings was allowed (*Golden Horse Shoe (New) v. Thurgood* (1933), 18 T.C. 280), being in the nature of stock-in-trade. (It will be noted that the materials contained in the "tailings" dumps have been separated from the soil while nitrate deposits have not.)

- (j) Loss of capital invested in a subsidiary company (*Jacobs, Young & Co. v. Harris* (1926), 11 T.C. 221). Revenue loss of subsidiary company (*Odhams Press v. Cook* (1940), T.R. 291).
- (k) Payment for the cancellation of a contract for the construction of a fixed asset ("*Countess Warwick*" *Steamship Co. v. Ogg* (1924), 8 T.C. 652).
- (l) Loss on realisation of shares taken up to secure contracts (*Stott v. Hoddinott* (1916), 7 T.C. 85).
- (m) Cost of unexecuted contracts taken over with a business (in arriving at the profits from the performance of the contracts) (*City of London Contract Corporation v. Styles* (1887), 2 T.C. 239).
- (n) Loss of money advanced to a managing director in excess of the commission due to him (*Roebank Printing Co. v. Commissioners of Inland Revenue* (1928), 13 T.C. 864).

- (o) Payment to lessor as consideration for surrender of lease of trade premises (*Cowcher v. Mills* (1927), 13 T.C. 216; *West African Drug Co. v. Lilley* (1947), T.R. 221), but rent in lieu of notice is allowed.
- (p) Dividends on shares held by directors (the Articles contained a provision that such dividends were to be regarded as part of the remuneration of the directors, but the shares were acquired by the directors for valuable consideration and were held unconditionally) (*Eyres v. Finnieston Engineering Co.* (1916), 7 T.C. 74).
- (q) The expenses of forming a company or raising its capital (*Texas Land and Mortgage Co. v. Holtham* (1894), 10 T.L.R. 337; 3 T.C. 255).
- (r) Directors' remuneration or other emoluments paid, particularly to members of the family, may be disallowed if as a fact they were not laid out wholly and exclusively for the purposes of the trade (*Copeman v. Wm. Flood & Sons* (1940), T.R. 491).
- (s) The excess of the market value over the issue price of shares allotted to employees (*Lowry v. Consolidated African Selection Trust* (1940), T.R. 299). "The cost to the company of earning its trading receipts was not increased by the issue of those shares at less than their full market value" (Lord Chancellor).
- (t) Medical expenses of a professional man (*Norman v. Golder* (1944), T.R. 335).
- (u) Payments made to persons about to retire from a company's service in consideration of restrictive covenants given by the persons retiring—on the grounds that permanent and solid benefits were acquired by the payments (*Assd. Portland Cement Manufactures v. C.I.R.* (1945), T.R. 347.)

#### (d) Removal Expenses.

Although expenses of removing business premises are not allowable deductions (*Granite Supply Association v. Kitton* (1905), 43 Sc. L.R. 65), a more lenient attitude is now adopted, and all removal expenses are allowed unless the removal arises as a result of mere business expansion, when the expenses to be

allowed will be considered on their merits. A circus proprietor, or the proprietor of a travelling business, is entitled to deduct his moving expenses (*Eastmans v. Shaw* and *v. C.I.R.* (1927), 14 T.C. 218, 225). The expenses of removing plant and machinery if not allowed as deductions from revenue, may be added to the cost of the asset for the purpose of computing the wear and tear allowance.

**(e) Bad Debts.**

All bad debts *bonâ fide* written off are permissible deductions. It is not unreasonable for the Inspector of Taxes to ask for details of the larger amounts written off, in order that he may check the position with the Inspector in the defaulting debtor's district, and such details are usually requested. Similarly, where specific debts are estimated to be wholly or partly doubtful, a reserve against the doubtful portion is allowable. A reserve against debts generally, e.g., on a percentage basis, is an appropriation of profit, however, and disallowed.

In practice, a debt is allowed to be written off as bad in the period in which it proves to be irrecoverable. It has been doubted whether this is in accordance with the law, but the *obiter dicta* in *Absalom v. Talbot* ((1944), T.R. 195) indicate that the practice has statutory support.

When reserves are written back to the credit of Profit and Loss Account, care must be taken to ensure that there is no double taxation. Bad debts recovered must be credited to the account (*Bristow v. William Dickenson & Co.* (1945), T.R. 295), and where a reserve against a specific debt is no longer necessary owing to the debt having been paid, this is equivalent to a recovery. Where, however, a reserve against debts

generally is reduced, the amount then credited to Profit and Loss Account has already been taxed, as the reserve was added back when set aside, hence the amount now written back should be deducted from the profits as already taxed.

Where a proper estimate is placed on a debt for the purpose of accounts and it is a reasonable estimate when made, it cannot be overthrown by any subsequent facts (*e.g.*, granting further credit to the debtor) which could justify the Commissioners in holding that the estimate was based on insufficient materials (*Anderton & Halstead v. Birrell* (1931), 16 T.C. 200; 10 A.T.C. 270).

Bad debts in respect of cash advances not laid out for the purpose of trade are not allowed (*English Crown Spelter Co. v. Baker* (1908), 5 T.C. 327), but if advanced for the purpose of trade the bad debt will be allowed (*Reid's Brewery Co. v. Male* (1891), 2 Q.B.1).

Where a company released a debt due to an associated company in order to give it relief—in effect, giving it new capital—on condition that the sum was to be applied in writing down its main asset, it was held that the amount was not a trading receipt of the latter company (*British Mexican Petroleum Co. v. Jackson* (1932), 16 T.C. 570).

Similarly, unclaimed balances standing to the credit of customers are not assessable when brought to credit of Profit and Loss Account (*Morley v. Tattersall* (1938), 22 T.C. 51).

#### (f) Hire Purchase Instalments.

Payments by a coal company to a wagon company under a hire-purchase agreement were held to be allowable in so far as the annual payments represented consideration for the use of the wagons (“interest”)



as distinct from payments for an option at a future date to purchase the wagons at a nominal price (*Darngavil Coal Co. v. Francis* (1913), 7 T.C. 1).

The "interest" portion of the annual instalment may be charged on either of these bases: (1) the total instalments less the cash price may be spread evenly over the period of the agreement, or (2) the amount of interest may be calculated annually on the basis explained in works on Book-keeping and Accounts (*e.g.*, see Spicer & Pegler's "Book-keeping and Accounts," Chapter XIV, § 1). Wear and tear allowance can be claimed by reference to the cash price. If wear and tear allowances are claimed on the full price, no portion of it can be claimed as interest.

**(g) Subscriptions to Trade Associations.**

Whether subscriptions or levies paid to a trade association are allowable depends on the purposes to which the association devotes the moneys so received. Generally speaking, if all the expenses incurred by the association are such as would properly be allowable if incurred by the contributories individually, the whole of the contributions and levies paid by the members would be allowable on satisfactory proof of the circumstances.

If the expenses of the association are partly admissible and partly inadmissible, an apportionment of the contribution may be necessary (*Lochgelly Iron & Coal Co. v. Crawford* (1913), 6 Tax Cas. 267).

In practice, it is customary for trade associations to sign an agreement to pay tax on the excess of their receipts over allowable expenses, in which case the whole of the payments made by members are allowed as a charge in the accounts of the members.

Each Inspector of Taxes has a list of the associations which have entered into such an agreement, and unless the association in question is on that list, the Inspector will resist the allowance of the contribution. In view of the difficulty of proving the relative proportions of the contributions applicable to the respective activities of such associations, the Inspector is usually successful if the matter is taken before the Commissioners. It is of vital importance that the exact and full name of the association be given to the Inspector in order to enable him to check whether it is on his list.

Subscription to a Coal Owners' Association, the object of which was to indemnify its members in the event of deficiency or stoppage of output caused by strikes, etc., was held to be not allowable as a deduction, on the ground that the payment was not money expended for the purpose of trade (*Rhymney Iron Co. v. Fowler* (1896), 2 Q.B. 79); but payment to a trade association formed for the purpose of keeping up prices was allowed, on the ground that the payment was exclusively made for the purpose of the trade (*Guest, Keen & Nettlefold, Ltd. v. Fowler* (1910), 5 T.C. 511).

**(h) Legal Expenses.**

Legal expenses of a revenue nature, *e.g.*, on debt recovery, are allowed as deductions, but the expenses of acquiring assets, *e.g.*, acquiring a lease, etc., are capital and not allowed. It is understood that the legal expenses on the renewal of short leases are now allowed, *i.e.*, provided the renewal is for less than 50 years. In general terms, the expenses of maintaining existing rights are allowed, but expenses of acquiring new rights are not. As to the exceptional position of brewers, see Chap. VI, § 3.

**(i) Contributions for National Insurance.**

Contributions under the National Insurance Act, paid by employers in respect of persons employed by them are allowable as a business expense.

**(j) Deduction from profits of contributions paid to rationalise industry (redundancy schemes).**

Where a person pays, wholly and exclusively for the purposes of a trade in respect of which he is chargeable under Case I, Schedule D, a contribution in furtherance of a scheme certified by the Board of Trade, the contribution, so far as it is paid in furtherance of the primary object of the scheme, is an allowable deduction in the accounts (§ 25—1935).

The Board of Trade must certify a scheme if they are satisfied—

- (a) that the primary object of the scheme is the elimination of redundant works or machinery or plant from use in an industry (including shipping) in the United Kingdom; and
- (b) that the scheme is in the national interest and in the interest of the said industry as a whole; and
- (c) that such number of persons engaged in the industry as are substantially representative of the industry are liable to pay contributions in furtherance of the primary object of the scheme by agreement between them and the body of persons carrying out the scheme.

The Board of Trade must cancel any certificate if they cease to be satisfied as to any of the above matters.

In the event of the repayment (whether directly or by way of distribution of assets on a winding-up or otherwise), of a contribution which has been allowed as a deduction, an additional assessment will be made under § 125, 1918, for the year in which the deduction was allowed. Such an additional assessment and any consequential assessment to sur-tax may be made at any time before the end of the third year following the year of assessment in which the repayment was made.

A sum received by any person by way of repayment of contributions is deemed to be by way of repayment of the last contribution paid by him, and, if the sum exceeds the amount of that contribution, by way of repayment of the penultimate contribution so paid, and so on.

The expression "contribution," in relation to a scheme, does not include a sum paid by a person by way of loan or subscription of share capital, or in consideration of the transfer of assets to him, or by way of a penalty for contravening or failing to comply with the scheme (§ 25—1935).

Schemes have also been sponsored by special Acts. The schemes provide for scrapping redundant works, plant or machinery, compensation being provided by levies on the industry.

As the original provision only had in view compensation to persons ceasing business as a result of the scheme, it did not provide for charging income tax on compensation received. To meet the case where all the concerns in an industry are scrapping portions of their plants and receiving compensation, it is now provided that payments on or after 6th April, 1945, are to be charged to Income Tax on the recipients as trading receipts, subject to deductions for payments made for damage not allowable under the Acts. If the recipient has ceased business, the receipt will be deemed to have been received on the last day on which he carried on the business. (An event which under Rule 11 of Cases I and II is to be treated as discontinuance is not to be regarded as discontinuance for this purpose) (§ 24—(No. 2) 1945.)

Where a scheme is cancelled after 20th December, 1945, sums available for repayment of contributions previously allowed, but not applied in such repayment within one year from the cancellation will be charged to tax under Case VI on the persons administering the scheme. If the contributions are subsequently repaid, the tax can be reclaimed (§ 25—(No. 2) 1945). The recipients will, of course, be liable. The aim is to prevent avoidance of tax by leaving surplus assets of

such funds in the hands of the persons administering the funds.

The above provisions of § 25 are applied also to statutory redundancy schemes (*e.g.*, those authorised under the Cotton Industry (Reorganisation) Act, 1939 (postponed by the Cotton Industry (Reorganisation) (Postponement) Act, 1939) when they come into force by Order in Council, with the necessary adaptations (§ 26—(No. 2) 1945).

(Rules for giving effect to § 24-26 above will be found in the Fourth Sch., Finance (No. 2) Act, 1945.)

**(k) Excess Profits Tax.**

Excess Profits Tax under the Finance (No. 2) Act, 1939, is allowed as a deduction for Income Tax purposes in the accounting period in respect of which it is payable.

Where Excess Profits Tax is repaid in respect of a deficiency, the amount must be treated as profit for Income Tax purposes for the year in respect of which it is received. Where, however, a deficiency of profits has been used to reduce unpaid E.P.T. of a previous period, the deduction for that earlier period is reduced accordingly (§ 18—(No. 2) 1939).

If E.P.T. or N.D.C. is adjusted for a past year, the Income Tax assessment based on the accounts affected is to be adjusted irrespective of the six years' normal time limit (§ 27—(No. 2) 1945).

Subject to certain undertakings and authorities, any amount by which the E.P.T. and N.D.C. paid for the period 1st April, 1940, to 31st December, 1945 (*i.e.*, the periods for which E.P.T. was 100%) exceeded the amount of E.P.T. and N.D.C. that would have been payable had E.P.T. been 80%, is to be refunded for use in developing and re-equipping specified businesses.

Tax is deducted from the refund at 9/- in the £, and the refund is regarded as part of the income of the year of assessment 1946-47 (§ 43—(No. 2) 1945).

The taxpayer may, however, claim not later than

5th April, 1947, or such extended period as the Commissioners of Inland Revenue allow, to spread the refund over the periods for which the refund accrued (§ 44—(No. 2) 1945). This may be very necessary in some cases, particularly where sur-tax is involved.

Alternatively, where the refund is to be used for the purposes of a business assessable for 1947-48 under Case I, notice may be given by all persons interested, not later than 31st December, 1948 (or extended period allowed by the Commissioners of Inland Revenue), electing to include the refund, in the income assessable in 1947-48 as business profits, provided some person who carried on the original trade is still carrying it on (alone or in partnership) throughout 1947-48. If there is a change in 1947-48 whereby the trade is deemed to be discontinued under Rule 11, the assessment will apply up to the date of discontinuance (§ 45—(No. 2) 1945).

Elaborate rules for making the spread are contained in §§ 44 and 50—(No. 2) 1945, but as these depend on E.P.T. law, they cannot adequately be included here. (They will be found in Wilson's "Winding up the E.P.T.")

**(1) Capital Expenditure on Rehabilitation Costs (§ 24—1947).**

This expenditure is deductible as an expense in computing profits for the purpose of Income Tax. "Rehabilitation costs" means expenditure on—

- (a) removal of works designed to afford protection from hostile attacks ;
- (b) moving a war-evacuated business back to its original or to a new home (not exceeding what would have been the cost of removal to the original home) ;
- (c) re-adapting plant, etc., to peace-time uses.

Such costs incurred in 1947, or if the C.I.R. are satisfied that circumstances justify the delay, in 1948 or 1949, will be allowed as deductions from profits. Any exceptional depreciation allowed will, of course, be adjusted to avoid double relief. Costs relieved under (c) above cannot be taken into account for wear and tear allowances, etc. Any grants in aid must be deducted from the costs.

**(m) Expenditure on Scientific Research.**

Where, after 6th April, 1946, a person carrying on a trade (not a profession)—

- (a) incurs expenditure not of a capital nature on scientific research related to that trade and directly undertaken by him or on his behalf; or
  - (b) makes a payment to any scientific research association for the time being approved for this purpose by the appropriate Research Council or Committee (being an association having as its object research related to that class of trade to which he belongs); or
  - (c) makes such a payment to any university, college, research institute or similar institution so approved,
- the expenditure is an allowable expense (§ 27—1944).

Any such payment made after 5th April, 1944, but on or before 6th April, 1946, which was disallowed when made, but is allowable under § 27, 1944, is to be treated as if it had been made on 7th April, 1946 (§ 44—I.T.A. 1945).

Capital expenditure on scientific research related to the trade, is to be allowed over five years, as follows :—

- (a) If incurred before the end of the year of assessment in which the business was commenced : One-fifth in the year of commencement and in each of the four following years.
- (b) If incurred in the year of assessment next following the date of commencement, but within 12 months from the commencement : One-fifth in that year of assessment and in each of the next four years.
- (c) If incurred after 12 months from the commencement and during the basis year for any year of assessment : One-fifth in that year of assessment and in each of the next four years.

Where two basis years overlap, any expenditure incurred in the period common to both is deemed to have been incurred in the first basis year only. If

there is an interval between the end of the basis year for one year of assessment and the beginning of the next basis year, any expenditure incurred in the interval is deemed to have been incurred in the second basis year. On the discontinuance of a trade, expenditure incurred before the end of the last complete year of assessment but after the end of the basis year for that year of assessment, is deemed to have been incurred in that basis year. The term "basis year" means the period to be taken as the year preceding the year of assessment (§ 28—1944).

Capital Expenditure on scientific research related to the trade and incurred on or after 1st January, 1937, but on or before 6th April, 1946, will rank for relief if the asset on which the expenditure was incurred still belonged to the trader and was still used for scientific research on 6th April, 1946 (§ 45—I.T.A. 1945). The expenditure, less any income tax allowances given up to and including 1945-46, will be treated as if it had been incurred immediately after 6th April, 1946, and allowed over five years.

#### Illustration.

Machine bought for scientific research for £1,000 in 1941; wear and tear allowances 1942-43 to 1945-46, £300 plus additional allowances £60. The balance of £640 is deemed to have been spent on 7th April, 1946, and annual allowances of £128 will be given in the assessments for 1947-48 to 1951-52.

Where an asset representing scientific research expenditure of a capital nature incurred by the person carrying on the trade ceases to be used by him for scientific research related to that trade—

- (a) No research allowance is permissible for any year of assessment after that in which the cessation takes place; and



- (b) Any excess of the capital expenditure over (i) the amounts allowed as above plus (ii) the value of the asset immediately before the cessation, is to be allowed as a deduction in charging the profits for the year of assessment in which the cessation takes place ; and
- (c) If in any subsequent year of assessment a claim is admissible for wear and tear, obsolescence, depreciation or exceptional depreciation, and the amount is dependent on the actual cost to the claimant of the asset, the cost of the asset or the net cost of the asset, then that cost, in determining whether any and, if so, what allowance is admissible, is to be treated as reduced by the amount of any deductions allowed under the last paragraph or (b) of this paragraph.
- (d) If appropriate, the “ industrial structure ” or “ wear and tear ” allowance under the Income Tax Act, 1945, will be given.

Where such an asset ceases to be used by the trader for scientific research related to his trade, and is then or later sold without having been used in the meantime for other purposes, then—

- (i) If an additional allowance would have been made under (b) above if the proceeds of sale had been regarded as the value of the asset, an amount equal to that allowance (less any in fact allowed) will be allowed in the year of assessment in which the sale occurs, or if the trade has then been discontinued for the ultimate year of assessment ;
- (ii) In any other case, if the proceeds of sale plus the total allowances made under § 28 *supra* and (b) above exceed the cost, the excess or the total of such allowances, whichever is the lesser, is to be regarded as a trading receipt at the date of sale, or if the business has ceased, immediately before the discontinuance.

For the purposes of (i) and (ii), if an asset is destroyed (from whatever cause (§ 46 (2)—I.T.A. 1945)), it is to be regarded as sold immediately before the destruction, and the insurance moneys or any compensation plus the proceeds of sale of the remains are to be regarded as the sale price.

If a deduction is allowed under these provisions, none is to be allowed for 1946-47 onwards, for wear and tear, obsolescence, depreciation or exceptional depreciation during the year of assessment during any part of which the assets are used for scientific research (§ 29—1944 ; § 46—I.T.A. 1945).

Deductions allowable under §§ 28 and 29 can be carried forward under the same rules as for wear and tear allowances, *i.e.*, there is no time limit, and § 19, 1932 applies where the allowance ousts losses (§ 30—1944).

The relief covers all expenditure for the prosecution of, or the provision of facilities for the prosecution of scientific research, except expenditure incurred in the acquisition of rights in, or arising out of, scientific research. Scientific research which may lead to, or facilitate an extension of the trade or trades of that class, and scientific research of a medical nature which has a special relation to the welfare of workers employed in the trade or class of trades, are included.

The appropriate Research Council or Committee is the Committee of the Privy Council for Scientific and Industrial Research, the Medical Research Council established under the Committee of the Privy Council for Medical Research, or the Agricultural Research Council established under the Committee of the Privy Council for Agricultural Research, as may be appropriate.

Expenditure met directly or indirectly by the Crown or any Government or public or local authority, whether in the United Kingdom or elsewhere, or by anyone other than the person carrying on the trade, is not included. Any dispute as to whether activities constitute, or an asset is used for scientific research

is to be referred by the Commissioners of Inland Revenue to the appropriate Research Council or Committee, whose decision is to be final (§ 31—1944).

**(n) Sale of Copyrights for lump sum.**

Where an author of a literary, dramatic, musical or artistic work assigns the copyright wholly or partially or grants an interest in it by licence, and the consideration for the assignment or grant consists wholly or partially of a lump sum which would hitherto have to be included in the profits of a single year of assessment, and the author was engaged on the making of the work for a period of over twelve months, a relief can be claimed for 1944-45 onwards as follows :—

*Period of Work.*

*Relief.*

If the author was engaged on the work for a period :—

(a) not exceeding 24 months :

To treat one-half of the payment as received on the actual date of receipt, the other half 12 months earlier.

(b) exceeding 24 months :

To treat one-third as received on the actual date of receipt, one-third 12 months earlier, and the remaining one-third 24 months earlier.

The claim must be made not later than 12 months from the end of the year of assessment in which the receipt is liable to be assessed. There is a right of appeal to the Special Commissioners. The term "author" includes a joint author, and the expression "lump sum payment" includes an advance on account of royalties which is not returnable (§ 24—1944).

Care must be taken, in deciding whether to make the claim, to compute the effect on all the years involved.

(As to deduction of tax from royalties paid to non-resident authors, *see* Chap. II, § 6 and Chap. IV, § 6.)

**(o) Trading with the Enemy.**

For 1939-40 onwards, any income that would be chargeable with income tax (including sur-tax) in the hands of an enemy is to be assessed on the custodian when received by him, and he must pay the tax out of the moneys in his hands belonging to the person in respect of whom he is assessed (including tax due for years prior to 1939-40) (§ 42 and Fourth Schedule—1944).

**(p) Repairs.**

Inspectors of Taxes frequently quote the case of *Law Shipping Co. v. C.I.R.* ((1923), 12 T.C. 621), in support of disallowing expenditure incurred in the early years of ownership of an asset. This case concerned a ship bought second-hand at a date when the periodical Lloyds' survey was overdue, having been deferred pending the completion of a contemplated voyage. On the return six months later, the survey was made and a large sum had to be spent in repairs. There was no succession to the trade of the vendors. It was held that only such part of the cost of the repairs as was attributable to the period during which the ship was employed in the company's trade was a proper deduction, the balance being in the nature of capital expenditure.

In another case, a company's only ship had been seized by the enemy during the war of 1914-18, and on its return in 1918, the company had to undertake extensive repairs, the cost of which was included in the claim made as damages against the enemy government. The claim was settled for about 45 per cent.

of its amount, and the sum recovered regarded as capital for tax purposes. The company claimed to deduct the cost of the repairs from their profits, but it was held that the necessity for the repairs had not arisen out of the use of the ship by the company in earning their profits, and was capital expenditure (*C.I.R. v. Granite City Steamship Co.* (1927), 13 T.C. 1).

It is essential to keep in mind the reason for the disallowance in both cases, *i.e.*, that the expenditure was not attributable to the use of the asset in the business. Accumulated repairs are allowable, so long as they have accumulated during the use of the asset. The *Law Shipping* case must not be too widely applied.

Any capital expenditure so incurred on an industrial structure will rank for allowances under the 1945 Act.

### § 3.—Adjustment of Accounts for Income Tax.

The customary method of adjusting the Profit and Loss Account in order to arrive at the correct figure of profit for Income Tax purposes, is as follows :—

Take the net profit as shown by the Profit and Loss Account, and (a) add the amounts charged in the Profit and Loss Account which are disallowed, and any trading income which has not been included in the Profit and Loss Account, and (b) deduct (i) those items of receipt upon which tax has already been paid by way of deduction, or which are not part of the trading profits or are assessable under any other Case or Schedule, or which are not subject to tax, and (ii) any allowable expenses which have not been debited in the accounts.

**Illustration (1).**

The following is the Profit and Loss Account of Charles Clarke & Co., for the year 1946. Show the Assessment for 1947-48.

PROFIT AND LOSS ACCOUNT			
<i>Dr.</i>	For the Year ended 31st December, 1946.		<i>Cr.</i>
To Rent. .. .. .	£ 40	By Gross Profit from Trading	£
" Salaries .. .. .	390	Account .. .. .	1,400
" Trade Expenses .. .. .	145	" Discount Receivable .. .. .	84
" Bad Debts .. .. .	68		
" Discount payable .. .. .	152		
" Income Tax .. .. .	31		
" Partner's Salary .. .. .	100		
" Bank Interest .. .. .	10		
" Interest on Capital .. .. .	75		
" Net Profit .. .. .	473		
	£ 1,484		£ 1,484

**INCOME TAX COMPUTATION.**

Net Profit as per above Account .. ..	£473
Add Income Tax .. ..	31
Partner's Salary .. ..	100
Interest on Capital .. ..	75
Assessable Profit .. ..	£679
Assessment 1947-48 .. ..	£679

*Notes to Illustration.*

- (1) The items "added back" are all appropriations of profits.
- (2) **BANK INTEREST.**—This is "short" not "annual" interest, and Income Tax is not therefore deductible on payment, with the result that the interest is an allowable deduction and the bank must include such interest in its profits. Where it is not allowable as an expense, a repayment of tax in respect of such interest may be claimed against tax paid (*see* Chap. IX, § 6).

When submitting accounts to Inspectors of Taxes a computation of the profits for Income Tax should be enclosed, so that the Inspector can see at a glance what adjustments have been made.

In the case of sole traders and partnerships, where the auditors do not give a "clean" certificate indicating that a complete audit has been made, the following form of certificate is usually required to be completed and returned to the Inspector of Taxes in support of the accounts :—

## INCOME TAX.

Name of Concern.....

Accounts for..... months ended.....194....

To H.M. INSPECTOR OF TAXES.

I hereby certify that to the best of my knowledge and belief,

- (a) All transactions relating to the business of .....were correctly entered in the books of account produced to Messrs.....
- (b) the whole of the stock-in-trade of the business (wherever situated) on .....was shown in the stock sheets produced to Messrs.....
- and (c) the statements below which relate to the accounts for the period above named are true.

(To be signed by the Proprietor  
or by the Precedent Acting  
Partner in a firm, or by the .....Signature.  
Managing Director of a  
Limited Company.)

.....Date.

- (1) Did any Reserves or Suspense Accounts exist (1)  
at.....that are not separately shown on the face of the Balance Sheet supplied to the Inspector of Taxes?  
If so, please give particulars.
- (2) Are the amounts shown as Purchases in the (2)  
accounts supplied to the Inspector of Taxes restricted to the cost of goods (a) sold and included in Sales in the Trading Account, or (b) forming part of the Stock of which the value is shown in the Balance Sheet?
- (3) (a) On what basis precisely was the Stock- (3) (a)  
in-Trade shown in the Stock Sheets valued?  
(b) Was this basis the same as that hitherto (b)  
adopted?  
(c) What was the full value of the Stock on (c)  
the basis stated above?  
(d) Please state particulars of any deduc- (d)  
tions that have been made from the full value of the Stock in arriving at the value shown in the Balance Sheet supplied to the Inspector of Taxes.

The certificate is not a statutory one and its completion cannot be enforced, but it is wise to comply with the Inspector's request.

(As to Farmers' Accounts, *see* Chap. VI, § 6.)

It is appropriate to note that the C.I.R., take the view that the lower of "cost or market value," which is the customary method of valuing stock, means that all stock must be valued on the same basis, *i.e.*, it is not permissible to take the lower value for each item, but the lower of total cost or total market value of all stock must be taken. (The C.I.R. refer to this as the "global" method.) Obsolete or damaged stock, however, need not be included, but may be valued on its own merits. What constitutes market value is a matter which is dealt with in works on Auditing. It should be stated that the Revenue view is not accepted by all businesses, many of whom value each item or group of items. It is considered that this is not a matter on which the C.I.R. should be allowed to interfere with the established practices of commercial usage. The Acts are silent on the point, and the matter is therefore, one for decision by Appeal Commissioners in the event of dispute. Over a long period, it does not matter which method applies, but it does affect yearly accounts. The method adopted should, of course, be consistent year by year. If the method is changed, the opening and closing stocks should be valued on the same basis. (*Cf. Brigg Neumann & Co. v. C.I.R.* (1928), 12 T.C. 1191; *Whimster v. C.I.R.* (1926), 12 T.C. 813; *Osborne v. Steel Barrel Co.* (1942), 1 A.E. 634; *Bombay Commissioners v. Ahmedabad New Cotton Mills* (1929), 8 A.T.C. 575.) In the case of finance companies, however, properties and investments are usually valued on the "global" method;



this has been upheld by the Special Commissioners on appeal.

(See also the Recommendations of the Institute of Chartered Accountants in England and Wales on the question of stock valuation.)

In the case of sole traders in particular, it is sometimes found that items not charged in the accounts are permissible deductions, *e.g.*, renewals may have been capitalised, or business expenses paid privately. This is frequently the case where part of a dwelling-house is used for the purposes of the business; a fair charge for rent (or annual value), rates, lighting, etc., is a proper deduction and should be adjusted. In the case of companies, it is not unusual to find in preliminary expenses some items which would be allowed, *e.g.*, the cost of books of account, etc.

The following is an illustration of the adjustment of the Profit and Loss Account of a Limited Company for Income Tax purposes:—

#### Illustration (2).

The following is the Profit and Loss Account of the Wholesale Trading Co., Ltd., for the year 1946. Show the Assessment for 1947-48. The Claim for Wear and Tear is admitted at £250; Renewals of Furniture for the year are £27, and have been capitalised.

Dr.	PROFIT AND LOSS ACCOUNT.		Cr.
To Trade Expenses .. ..	£ 2,250	By Gross Profit .. ..	£ 4,006
" Annuity .. ..	200	" Dividends received .. ..	120
" Depreciation of Plant .. ..	300	" (less tax)	
" " " Furniture .. ..	51	" Bank Interest received (Gross)	95
" Rent .. ..	500	" Balance, being Loss .. ..	6,250
" Income Tax .. ..	1,140		
" Loss on Sale of Investments .. ..	30		
" Loss by Embezzlement .. ..	400		
" Debenture Interest .. ..	5,000		
" Directors' Fees .. ..	500		
" Income Tax on Directors' Fees .. ..	100		
	<u>£10,471</u>		<u>£10,471</u>

## INCOME TAX COMPUTATION.

Loss as per Accounts	.. ..	£6,250
<i>Add</i> : Dividends Received	.. ..	120
Bank Interest Received	.. ..	95
Renewals of Furniture	.. ..	27
		<u>6,492</u>
<i>Deduct</i> : Annuity	.. ..	£200
Depreciation of Plant	.. ..	300
"      " Furniture	.. ..	51
Income Tax	.. ..	1,140
Loss on Investments	.. ..	30
Debenture Interest	.. ..	5,000
		<u>6,721</u>
Assessable Profit	.. ..	<u>£229</u>
Profit, 1946	.. ..	£229
Less Claim for Wear and Tear, 1947-48	.. ..	250
		<u>Nil.</u>
Assessment 1947-48, Case III, Schedule D		£95
Wear and Tear carried forward to 1948-49		£21

NOTE.—As will be seen later—Chap. IV, § 6—an assessment will be raised under General Rule 21, on the amount of the debenture interest and annuity paid in 1947-48 in so far as it is not covered by income taxed at source or under other Schedules or Cases. Bank interest received is sometimes not adjusted but left in the profits in lieu of being assessed under Case III.

The method of adjustment should be noted. Since there is a loss on the Profit and Loss Account, this must be increased by the credit items that are not part of the trading profit and decreased by the disallowable expenses. The result is an adjusted profit.

#### § 4.—Machinery and Plant—Allowances.

(a) *Initial Allowances* (§ 15—I.T.A. 1945).

As from 6th April, 1946, any capital expenditure on machinery and plant will rank for an initial allowance of 20 per cent. The allowance is given in the same way as the wear and tear allowance (see (b)

below), *i.e.*, as a deduction in the assessment for the year of assessment in the basis period for which the expenditure was incurred. The basis period is, of course, normally the accounting period ended in the preceding year of assessment.

To avoid double allowances in the cases where the assessment is based on the profits of an “actual” or some other period, it is provided that—

- (a) Where two basis periods overlap, the period common to both is deemed to fall in the first basis period only. If two periods are coincident, or one is included in another, they overlap (§ 68 (5)—I.T.A. 1945).
- (b) Where there is an interval between the basis period for succeeding years of assessment, then, unless the second year of assessment is the year of discontinuance, the interval is deemed to be part of the second basis period.
- (c) If in (b) the second year of assessment is the year of discontinuance, the interval is deemed to fall into the first basis period (§ 57—I.T.A. 1945).

The Initial Allowance is 20 per cent. of the Capital Expenditure.

#### Illustration (1).

(a) Expenditure in May, 1946, will be in the basis period for 1947-48, in a continuing business.

(b) Business started 1st June, 1946, making up accounts to 31st December, 1946 and 1947.

The assessment will be as follows (*see* Chap. IV, § 8):—

1946-47—Profits to 31/12/46 plus three months proportion of the 1947 profits.

1947-48—Profits to 31/12/46 plus five months proportion of the 1947 profits.

1948-49—Profits of 1947.

Any expenditure up to 5th April, 1947, will be regarded as falling in the first basis period, and initial allowances given in 1946-47; expenditure from 6th April, 1947, to 31st May, 1947, will rank for initial allowance in 1947-48; and expenditure from 1st June, 1947, to 31st December, 1947, for allowance in 1948-49.

(c) Accounts made up to 31st December, until 1949, then a fifteen months' account to 31st March, 1951. Assessment for 1950-51 based on the 1949 accounts; that for 1951-52 on 12/15ths of the the accounts to March 1951. Any expenditure between 1st January, and 31st March, 1950, would be regarded as in the basis period for 1951/52.

(d) Accounts made up to 31st December, 1948, and 1949, then a seven months' account to the date of discontinuance, 31st July, 1950. Assessment for 1949-50 based on the 1948 accounts; that for 1950-51, on that proportion of the accounts for the seven months which falls after 5th April, 1950, say 4/7ths.

Any expenditure from 1st January, 1949 to 5th April, 1950, will rank for initial allowance in 1949-50.

Capital Expenditure on plant and machinery incurred on or after 6th April, 1944, but before 6th April, 1946, will rank for initial allowance as if there had been expended on 6th April, 1946, the amount actually expended during the said period, less any allowances given for income tax purposes up to 5th April, 1946. It is a condition of the allowance that the plant, etc., was owned on 6th April, 1946, by the person who incurred the expenditure and was in use on that day and not worn out, obsolete or otherwise useless or no longer required.

#### Illustration (2).

Plant bought April-December, 1944	..	..	..	£5,000
Less Wear and Tear allowed 1945-46	..	..	..	600
				<hr/> 4,400
Plant bought 1945	..	..	..	3,000
Plant bought 1st January-5th April, 1946	..	..	..	1,000
				<hr/> 1,000
Amount deemed to have been spent on 6th April, 1946				<hr/> <hr/> £8,400

As 6th April, 1946, will be in the basis period for the year of assessment 1947-48, the initial allowance will be given in 1947-48—20% of the £8,400 = £1,680.

(In exceptional cases, of course, the special rules mentioned above will fix the basis period, *i.e.*, where there has been a change in the accounting date or in the case of a new or discontinued business.)

Initial allowances apply to professions, etc., assessed under Case II, and to employments, etc., assessed under Sch. E. Under Sch. E., of course, the assessment being on the actual profits of the year of assessment, the initial allowance is given in the year in which the expenditure is incurred.

Where there is a contract for the sale of a ship and the price became payable before 6th April, 1946, but the ship was delivered later, or the price is payable by instalments, some before that date, some on or after it, then any part of the price paid before 6th April, 1946, is deemed to have been paid on that date.

Otherwise, expenditure is deemed to be incurred on the date on which it becomes payable (§ 62—I.T.A. 1945). In all cases, grants from Government Depts., Local Authorities or any other person, directly or indirectly, towards the cost, are deductible from the expenditure, *i.e.*, the allowance is on the net cost. In certain circumstances, the contributor may get allowance (§ 66—I.T.A. 1945).

*(b) Allowances for Wear and Tear and Obsolescence.*

(Sch. D, Cases I and II, Rules 6 and 7; § 16—1925; §§ 16-24—I.T.A. 1945).

In assessing profits or gains of any trade, profession, vocation, employment or office (and profits from lands, including woodlands, under Sch. D or Sch. B, R. 6) the assessing Commissioners may allow such

DEDUCTION AS THEY MAY THINK JUST AND REASONABLE, AS REPRESENTING THE DIMINISHED VALUE BY REASON OF WEAR AND TEAR, of any MACHINERY OR PLANT USED at the end of the basis period for the purposes of the concern and BELONGING TO THE PERSON or company by whom the concern is carried on.

In practice an allowance can usually be obtained on trade fixtures and fittings as well as pure plant.

Where machinery or plant is let, and the lessee is bound to deliver it up at the expiration of the lease in good condition, the plant will be regarded, for the purpose of wear and tear, as belonging to the lessee. If the burden of maintaining the plant falls on the lessor, he is entitled to make a claim for repayment of tax in respect of wear and tear of the plant, but such claim must be made within twelve calendar months after the expiration of the year of assessment. A lessee is not entitled to the allowance unless the assessing Commissioners are satisfied that the burden of the wear and tear will fall directly on him (§ 22—1940). The allowance to the lessor, where appropriate, is for so much of the period of letting as falls within the year of assessment, and on so much of the plant, etc., as is in use at the end of the year (§ 20—I.T.A. 1945).

It is given mainly against income from the letting, but any excess may be set against other income (§§ 23, 56—I.T.A. 1945).

The wear and tear allowance should be claimed in the Income Tax return for the year, even where there are no assessable profits, in view of the "carry forward" provisions. An "error or mistake" claim, can however, be made to remedy the failure to claim the allowance except where no Return has been made. (See Chap. II, § 31.)

All allowances granted for 1938-39 to 1945-46 were increased by one-fifth of themselves (from 1932-33 to 1937-38 by one-tenth) (§ 18—1932 ; § 22—1938). As from 6th April, 1946, all allowances are increased by 25% (§ 16—I.T.A. 1945), *i.e.*, the allowance is now five-fourths of the old normal rates.

In a trade that consists of or includes the working of a mine, oil well or other source of mineral deposits of a wasting nature, the person carrying it on may elect that, instead of the allowance being five-fourths of the basic rate, it shall be such sum as the Commissioners consider to be just and reasonable, having regard to the date on which the source is likely to cease to be worked and the probable value of the plant, etc., at that date to the business (§ 16 (2)—I.T.A. 1945).

Repairs to plant (including renewals of small parts) can be charged to revenue without prejudice to the Wear and Tear Allowance, but renewals which substantially affect the identity of the machine are capital expenditure ranking for initial and wear and tear allowances.

The cost of altering an existing building incidental to the installation of plant, etc., is to be included as part of the cost of the plant, etc. (§ 21—I.T.A. 1946). This applies only to expenditure since 5th April, 1944.

Wherever plant is discarded or sold, it must be taken out of the Wear and Tear computation at its written down value. In respect of years of assessment up to and including 1945-46, if the plant was replaced, it was possible to claim an *Obsolescence Allowance*. In arriving at the adjusted profits of the year in which the plant was replaced, there could be deducted as an expense incurred in that year SO MUCH OF ANY AMOUNT EXPENDED in that year IN REPLACING ANY OBSOLETE PLANT OR MACHINERY AS WAS EQUIVALENT TO THE COST OF THE PLANT OR MACHINERY REPLACED after DEDUCTING from that cost the total amount of any WEAR AND TEAR ALLOWANCES already granted (including the additional "tenths" and "fifths") AND any sum REALISED BY THE SALE of that machinery or plant.

The cost of the new machinery was then treated as an addition to the plant.

Where two or more items were replaced, and one realised more than the residue of cost less allowances made, such surplus was not to be set against the corresponding deficiencies on other items. Each item had to be treated separately (*Charente Steamship Co. v. Wilmot* (1941), T.R. 247).

As from 6th April, 1946, the obsolescence allowance can no longer be claimed on new plant, etc. Instead, wherever plant, etc., is sold, or scrapped, there will be a "balancing allowance" (or "balancing charge," as may be appropriate). The balancing allowance (or charge) also applies to the plant, etc., purchased before and replaced after that date, but the taxpayer has the right, in respect of such plant, to claim the obsolescence allowance instead of having a balancing allowance (§ 18 (2)—I.T.A. 1945). These balancing adjustments are dealt with in § 3 (b) below.

The rate of wear and tear allowance varies according to the class of machinery and plant.

The allowance is for the year of assessment and is therefore deducted in the assessment, and not as an expense in the accounts. It is computed according to the "diminishing instalment" system of depreciation, *i.e.*, it is calculated on the cost price less all previous allowances. The "tenths" and "fifths," allowable up to 5th April, 1946, are NOT normally deducted in arriving at the written down value, but are added to the allowances calculated on the written down value. In the case of ships, the allowance is always a percentage of the prime cost, and not of the diminishing balance. (The "percentage of prime cost" method may be adopted for other plant, etc., but the rate of allowance will then be reduced; it



is rarely adopted.) As from 6th April, 1946, the increased allowance (five-fourths of the original rate) is deducted in arriving at the written down value.

Since assessments are normally based on the profits of the preceding year, it is convenient to base the wear and tear allowance on the value of the plant as at the end of the preceding accounting period, and it has always been the practice, and is now the law, to ignore changes in the plant, etc., after that date, but prior to the following 6th April. This procedure is made more necessary by the fact that the allowance has to be claimed in the return made at the beginning of the year of assessment. While up to 1945-46 additions, etc., could legally be, and in practice sometimes were, taken into account in the year in which they occurred, such a procedure was most inconvenient.

The capital value of the plant, etc., upon which the allowance is calculated normally differs from that appearing in the books of the business, owing to differences in dates of account, rates of depreciation, etc.

The allowance is given in the year of assessment in the basis period for which the expenditure is incurred. The rules for determining the basis period are the same as those for the initial allowance (*see* § 3 (a) above). In the case of the first year of assessment of a new business, therefore, the allowance is claimed on the capital expenditure on plant, etc., in that year.

Additions during the accounting year are brought into the computation for the purpose of allowance in the *following* year of assessment, the written down value of plant discarded or sold being deducted.

In the case of plant, etc., provided on or after 6th April, 1946, any contributions towards the cost met directly or indirectly by the Crown, Government department, local authority or any other person,

must be left out of account (§ 16 (3)—I.T.A. 1945). Prior to that date, contributions by third parties did not reduce the “cost price” to the person buying the plant (*Birmingham Corporation v. Barnes*, (1935), A.C. 292).

In the case of plant, etc., provided on or after 6th April, 1946, the wear and tear allowance is calculated on the “capital expenditure still unallowed” as at the beginning of the year of assessment (§ 16 (3)—I.T.A. 1945). This is the written down value, found by deducting from the capital expenditure, the allowances already made to the claimant for—

- (a) Initial allowance ;
- (b) Wear and tear ;
- (c) Exceptional depreciation ;
- (d) Scientific Research allowance ;
- (e) Balancing allowance.

Where full effect cannot be given to the deduction for initial and wear and tear allowances in any year, owing to there being no profits or gains chargeable for that year, or to the profits or gains chargeable being less than the allowances, the balance is carried forward and added to the wear and tear allowance of the following year, and any unutilised balance carried forward to the year next following, and so on until the allowance is exhausted.

Where there is a change in ownership of a business, the successor cannot claim his predecessor's unexhausted wear and tear allowances, except in the case of a partnership treated as a continuance of the same business (see Chap. IV, § 10).

In no case can the total allowances for wear and tear (including the additional “tenths” or “fifths”) exceed the cost price of the machinery or plant to the claimant. Accordingly, no deduction for wear and

tear, or repayment on account of any such deduction, can be allowed in any year, if the deduction, when added to the deductions allowed in any previous years to the person by whom the concern is carried on, will make the aggregate amount of the deductions exceed the actual cost to that person of the machinery or plant (including capital expenditure on the machinery or plant by way of renewal, improvement, or re-instatement).

The books forming part of a solicitor's law library are not plant and machinery within the meaning of the Rules governing wear and tear and obsolescence (*Daphne v. Shaw* (1926), 11 T.C. 256).

Where a person has failed to produce accounts, and has been assessed at an estimated amount, the wear and tear allowance is deemed to have been taken into account in the estimate, with the result that future allowances will be calculated as if the wear and tear allowances had been granted for the years of the estimates. Similarly, a Sch. B assessment is deemed to be the final figure of assessment for the year, and in the event of a claim for wear and tear allowance in any year by a person in respect of lands (including woodlands), the appropriate allowance is deemed to have been allowed for any previous year for which the profits were assessed under Sch. B (§ 16—1925). No initial, wear and tear, etc., allowance can be given in respect of an asset that ranks for relief under the agricultural land and buildings provisions of the 1945 Act (§ 24—I.T.A. 1945).

A Schedule of Special Rates of allowances for wear and tear of plant and machinery, fixed by agreement with regard to certain trades will be found in Appendix II. These must be increased by 25% for 1946-47 onwards.

**Illustration (1).**

The accounts of the Atlas Co., Ltd., as adjusted for the purposes of Income Tax assessment under Schedule D, but before deducting any claim for obsolescence, showed the following results:—

Years ended 31st December: 1943—£220; 1944—£990;  
1945—£1,140.

Prior to the year of assessment 1944-45, the assessable profits had been in excess of the allowance for Wear and Tear.

The written down value of the plant and machinery at 5th April, 1944, was taken for Income Tax purposes at £5,000. The rate of allowance was fixed by the Commissioners at 5%. Additional allowances then amounted to £53.

During 1944, additions amounting to £300 were made to the Plant, and also during 1944 a machine which had cost £1,000 in 1941 was scrapped as obsolete, realising £40 on sale. This machine was replaced at a cost of £1,400 in 1945.

Show what were the assessments under Schedule D for the years 1944-45, 1945-46 and 1946-47.

**CLAIMS FOR WEAR AND TEAR AND OBsolescence.**

			Additional 'Fifths.'	Total Allowance.
Written down value, 5th April, 1944	..	£5,000	£53	
Claim, 1944-45	.. .. .	250	+	50
		<hr/>		<hr/>
		4,750		103
Additions, 1944	.. .. .	300		
		<hr/>		
		5,050		
Less. Machine Sold. available for Obsolescence Claim when replaced (see below)		857	+	29
		<hr/>		<hr/>
Written down value, 5th April, 1945	..	4,193	-	74
Claim, 1945-46	.. .. .	210	+	42
		<hr/>		<hr/>
		3,983		
Addition, 1945	.. .. .	1,400		
		<hr/>		
		5,383		
Claim, 1946-47, $6\frac{1}{4}\%$	.. .. .	336		336
		<hr/>		<hr/>
Written down value carried forward	..	£5,047	-	£116

## COMPUTATION OF WRITTEN DOWN VALUE OF MACHINE SCRAPPED.

Cost, 1941 .. .. .	£1,000	
Claim, 1942-43 .. .. .	50	+ £10
	<u>950</u>	
Claim, 1943-44 .. .. .	48	+ 10
	<u>902</u>	
Claim, 1944-45 .. .. .	45	+ 9
	<u>£857</u>	- <u>£29</u>

## COMPUTATION OF OBSOLESCENCE CLAIM.

Original Cost of Machine scrapped .. .. .	£1,000
<i>Deduct: Wear and Tear Allowed</i>	
£ (50 + 48 + 45 + 29) .. .. .	£172
Proceeds of Sale .. .. .	40
	<u>212</u>
Obsolescence Claim (£857 - 29 - 40) =	<u>£788</u>

(NOTE.—Had the new machine cost less than £788, only the cost would have been allowed.)

## ASSESSMENTS.

			Wear and Tear carried forward.
1944-45—Profits of 1943 .. .. .	£220		
Less Wear and Tear (part) .. .. .	220		£80
	<u>Nil.</u>		
1945-46—Profits of 1944 .. .. .	£990		
Less Wear and Tear—			
1945-46 .. .. .	£252		
Brought forward .. .. .	80		
	<u>332</u>		
Assessment .. .. .	<u>£658</u>		
1946-47—Profits of 1945 .. .. .	£1,140		
Less Obsolescence Claim .. .. .	788		
	<u>352</u>		
Less Wear and Tear, 1946-47 .. .. .	336		
	<u>£16</u>		

There is no limit to the period during which unexhausted Wear and Tear Allowances may be carried forward; they can be

so treated until utilised as deductions. On the other hand, it is not permissible to "miss" a year (*e.g.*, where the assessable profit is so small that it would be absorbed by other allowances); wherever there is an assessable profit the Wear and Tear Allowance will be deducted, and only the unabsorbed balance carried forward. (*See* Chap. VII, § 2, as to losses.)

Where the plant account for wear and tear purposes was kept on an "additions less sales" basis (plant scrapped not being identified), the tenths or fifths *had to be* subtracted *each year* in arriving at the written-down value. In all cases, the taxpayer could continue on the basis of including the whole allowance in arriving at the written-down value if he so chose.

In the case of a new business, proper assessments cannot be raised until the first year's accounts are available, and it is therefore perfectly convenient, and the practice, to give an allowance on the actual plant for the first year, or the first two years if the plant is acquired gradually.

#### Illustration (2).

Business commenced 1st January, 1942. Plant bought on 1st January, 1942, £5,000; 1st April, 1942, £10,000. Wear and Tear Allowance at  $7\frac{1}{2}\%$ .

#### WEAR AND TEAR COMPUTATION.

	£	Additional "Fifths."	Total.
Cost 1st January, 1942 .. .. .	5,000		
Allowed 1941-42, $7\frac{1}{2}\%$ for 3 months	94	£19	£113
	<hr/> 4,906		
Addition, 1st April, 1942.. .. .	10,000		
	<hr/> 14,906		
Allowed, 1942-43, $7\frac{1}{2}\%$ .. .. .	1,118	224	1,342
	<hr/> 13,788		
Allowed, 1943-44 .. .. .	1,034	207	1,241
	<hr/> £12,754		
Written down value carried forward ..	<u>£12,754</u>	- <u>£450</u>	

Where no Wear and Tear allowance is claimed, the cost of renewals will be allowed as a charge in the year of replacement. This is actually an obsolescence allowance, and is the lower of (a) the cost of the new plant, or (b) the cost of the old plant less proceeds of sale.

Where a shop front is replaced, the allowance for replacement is limited to what would have been the cost of replacing the old front by a similar one. Wear and tear cannot be claimed on the capital expenditure represented by improvements.

(c) *Balancing Allowances and Balancing Charges*  
(§ 17—I.T.A. 1945).

Prior to 6th April, 1946, if plant, etc., was sold for more than its written down value, the profit was a capital one, and could not be assessed. As from that date, however, whenever plant, etc., realises more than its written down value, a balancing charge can be made to take away the excess allowances deemed to have been made in the past. There can, however, be no charge on any amount by which the sale price exceeds original cost; the maximum balancing charge is the allowances already given.

**Illustration (1).**

	(1)	(2)
Plant bought 1946, cost .. .. .	£10,000	£10,000
Initial Allowance, 1947-48 .. .. .	£2,000	
Wear and Tear Allowance 1947-48		
$\frac{1}{4} \times 10\% \dots\dots\dots$	1,250	
	<u>3,250</u>	£3,250
	6,750	
Wear and Tear Allowance 1948-49 .. .. .	844	844
	<u>5,906</u>	
Wear and Tear Allowance 1949-50 .. .. .	738	738
	<u>5,168</u>	5,168
Sold in 1949 for .. . . .	8,000	11,000
	<u>£2,832</u>	<u>£5,832</u>
Balancing charge, 1950-51 .. . . .	<u>£2,832</u>	<u>£4,832</u>

In the second case, the charge takes away the excess allowances made, but cannot include the true capital profit of £1,000.

In the case of a lessor, a balancing charge is assessed under Case VI.

Where there is an arrangement for unification or grouping of cotton or staple rayon fibre spinning concerns, and the Board of Trade certify that the arrangements satisfy the conditions for a re-equipment grant, only half the standard rate is to be charged on any balancing charge on machinery sold before 6th April, 1950, by one party to another in the carrying out of the arrangements (§ 18—1947).

Prior to 6th April, 1946, if plant was sold for less than its written down value, no allowance was given at all for the difference, unless the plant was replaced, in which case the obsolescence allowance applied. This again is changed, and whenever plant is sold or scrapped after 6th April, 1946, a balancing adjustment is made.

**Illustration (2).**

If the plant in the previous illustration were sold in 1949 for £3,000, a balancing allowance would be made in 1950-51 of £2,168 in each case.

The balancing allowance or charge applies where—

- (a) the plant is sold, whether while still in use or not ; or
- (b) the plant ceases to belong to the trader, owing to a foreign concession coming to an end ; or
- (c) the plant is destroyed ; or
- (d) the plant is put out of use as worn out, obsolete, useless or no longer required,

provided the event occurs before the trade is permanently discontinued. (A business is *not* “ permanently discontinued ” for this purpose where there is a change of ownership, which is deemed under Rule 11 (Cases I and II) (*see* Chap. IV § 10) to amount to discontinuance.)



Where the wear and tear allowances on a mine, etc., are calculated on output, the balancing allowance or charge will be made even if the event is discontinuance; the same applies where the event is the coming to an end of a foreign concession.

Sale, insurance, salvage or compensation moneys must be regarded as proceeds of sale, except that where the loss of a ship is due to a war risk, there is to be no balancing charge by reason of the loss (§ 17 (3)—I.T.A. 1945).

Grants from the Crown, etc., are excluded from the cost price except for the purpose of a balancing charge on plant provided before 6th April, 1946 (§ 66—I.T.A. 1945).

Balancing charges and allowances are made in the same way as wear and tear allowances, *i.e.*, by addition to, or deduction from, the assessment for the year of assessment of which the period in which the plant is sold or ceases to be used forms the "basis period."

As an alternative to a balancing charge, a taxpayer who replaces an item of plant, may claim to deduct from the cost of the replacement the amount on which a charge is due. If the charge due to be made exceeds the cost of the replacement, the balancing charge will be made on the excess and no allowances whatever given on the replacement until it in turn is sold or scrapped, when a balancing allowance or charge will be made as if there was a written down value of nil.

If the charge is less than the cost of the replacement, the charge will be deducted in arriving at the written down value of the replacement, and the initial wear and tear allowances given on the balance.

## Illustration (3).

	(1)	(2)
Plant Cost 1946 .. .. .	£10,000	£10,000
Initial Allowance 1947-48 .. £2,000		
Wear and Tear Allowance 1947-48		
$\frac{1}{5} \times 5\%$ .. .. .	625	
	<u>2,625</u>	£2,625
Wear and Tear Allowance 1948-49 ..	7,375	
	<u>461</u>	461
Wear and Tear Allowance 1949-50 ..	6,914	
	<u>432</u>	432
		<u>3,518</u>
Proceeds of Sale, 1949 .. .. .	6,482	6,482
	<u>9,000</u>	<u>7,000</u>
Balancing Charge due .. .. .	£2,518	£518
Cost of replacement .. .. .	£2,400	£2,400
Deduct Balancing Charge due ..	<u>2,518</u>	<u>518</u>
Balancing Charge made in 1950-51 ..	£118	£1,882
Initial Allowance 1950-51 .. ..	—	376
Wear and Tear Allowance 1950-51 ..	—	<u>118</u>
		494
Wear and Tear Allowance 1951-52 ..	—	<u>1,388</u>
		87
		<u>87</u>
Wear and Tear Allowance 1952-53 ..	—	1,301
		<u>81</u>
		<u>81</u>
		<u>1,220</u>
Plant scrapped 1952 sold for .. ..	500	500
	<u>+ £500</u>	<u>- £720</u>

In case (1), there will be a balancing charge of £500 in 1953-54, as the whole of the expenditure has been allowed ; in (2) a balancing allowance of £720.

	(1)	(2)
Proof: Cost of first asset .. .. .	£10,000	£10,000
Cost of second asset .. .. .	2,400	2,400
	<u>12,400</u>	<u>12,400</u>
Less Proceeds of sales :		
First .. .. .	£9,000	£7,000
Second .. .. .	<u>500</u>	<u>500</u>
	9,500	7,500
Amount to be allowed .. .. .	<u>£2,900</u>	<u>£4,900</u>

## Amounts allowed :

First .. .. .	£3,518		£3,518
Second .. .. .	—		662
	<hr/>		<hr/>
	3,518		4,180
Balancing Charges .. .. .	618	Allowance	720
	<hr/>		<hr/>
Total allowed .. .. .	£2,900		£4,900
	<hr/>		<hr/>

In the case of plant bought before 6th April, 1946, but after 5th April, 1944, so that it qualifies for initial allowance, there is a difference of opinion as to the interpretation of the Act in regard to the treatment of the additional “fifths” allowed up to 5th April, 1946. The official view is that they must be deducted in arriving at the written down value for the initial allowance but not for wear and tear allowance calculations. They must, of course, be deducted in computing the amount of the balancing adjustment.

**Illustration (4).**

Plant bought 1944 .. .. .	£10,000		
Wear and Tear Allowance 1945-46			
at $7\frac{1}{2}\%$ .. .. .	750	+	150
	<hr/>		<hr/>
	9,250	-	150
Wear and Tear Allowance 1946-47			
$\frac{5}{4} \times 7\frac{1}{2}\% = 9\frac{3}{8}\%$ .. .. .	867		
	<hr/>		<hr/>
	£8,383	-	150
Initial Allowance 1947-48			
20% of £9,250 - £150 .. .. .	1,820		
Wear and Tear Allowance 1947-48			
$9\frac{3}{8}\%$ of £8,383 .. .. .	786		
	<hr/>		<hr/>
	2,606		
	<hr/>		<hr/>
	5,777	-	150
Wear and Tear Allowance 1948-49 .. .. .	542		
	<hr/>		<hr/>
	5,235	-	150
	<hr/>		<hr/>
Proceeds of sale when scrapped in 1948	£250		
Additional “fifths” .. .. .	150		
	<hr/>		<hr/>
	400		
Balancing Allowance .. .. .	£4,835		
	<hr/>		<hr/>

Where assets are transferred to the National Coal Board under the Coal Industry Nationalisation Act, 1946, the provisions of the 7th Schedule to the 1947 Act have effect in computing the liability to tax of the previous owner and the Board respectively (§ 29—1947). Broadly, the date of the transfer of the assets is substituted for 6th April, 1946, as the “appointed day” under the Income Tax Act, 1945, and the vesting of any relevant property should not be treated as a sale or a purchase for any of the purposes of the Income Tax Act, 1945. As this has only limited application, the schedule is not reproduced.

*(d) Miscellaneous points under the Income Tax Act, 1945.*

To prevent taxpayers from making arrangements that would attract allowances under the Act, it is provided (§ 59—I.T.A. 1945) that where either—

- (a) the buyer is a body of persons over whom the seller has control (see below), or the seller is a body of persons over whom the buyer has control, or both the seller and the buyer are bodies of persons and some other person has control over both of them; or
- (b) it appears with respect to the sale or with respect to transactions of which the sale is one, that the sale or main benefit which, apart from the provisions of § 59 (which is now being considered), might have been expected to accrue to the parties or any of them was the obtaining of an allowance or deduction under the 1945 Act, or for wear and tear or for exceptional depreciation or for scientific research expenditure, the following restrictions apply :—

(1) If the sale is at a price other than what the asset would have fetched if sold in the open market (the valuation to be at the earlier of the time of completion or time when possession was given (§ 68)), allowances, etc., are to be calculated as if the asset had been sold at the open market price, or the “limit of re-charge” to the seller, whichever is less. If, however, the plant has never been used and is sold by the manufacturer or supplier of plant in the ordinary course of business, the “limit of re-charge” provision does not apply, and only the open market value is regarded. Moreover, if the sale took place before 6th April, 1946, and the seller acquired the plant after 5th April, 1944, only the open market sales value is regarded if (a) above applies, though if (b) applies, the “limit of recharge” must be taken into account.

The limit of recharge means—

- (i) if the seller provided the plant for himself before 6th April, 1946, the actual cost to him (including any capital expenditure by way of renewal, improvement or reinstatement);
- (ii) if he provided the plant on or after 6th April, 1946, the actual expenditure incurred.

(2) If the transaction is within (b) above, no initial allowance will be made to the buyer. If, however, it is within (a) above (and not caught by (b)), and—

- (i) the seller has had an initial allowance when he provided the plant, and
- (ii) a balancing charge is made on the seller, and
- (iii) the open market value of the plant at the time of the sale exceeds four-fifths of the limit of recharge on the seller; then the buyer will be entitled to an initial allowance not exceeding the lowest of—
  - (a) the excess of the open market price over four-fifths of the limit of recharge;
  - (b) the initial allowance already made to the seller;
  - (c) the balancing charge on the seller (§ 34—1946);otherwise no initial allowance will be made.

(3) Where (a) above applies and (b) does not, the parties to the sale may, however, elect that there be substituted for the open market price, the capital expenditure still unallowed immediately before the sale, if that is lower than the open market price, in which case the limit of recharge provisions do not apply. In calculating the expenditure still unallowed, provisional exceptional depreciation allowances are left out of account. If this option is exercised then when the buyer subsequently scraps or sells the plant, such balancing charge (if any) will be made on him as would have fallen to be made on the seller if he had continued to own plant and has had all the allowances subsequently made to the buyer.

Control, for the above purposes, in relation to a company, means the power to secure, by shareholding or voting power, or powers conferred by the Articles of Association or other document regulating any company, that the affairs of the company are conducted in accordance with the wishes of the person concerned, or in the case of a partnership, the right to more than half the assets or more than half the income of the partnership (§ 68—I.T.A. 1945).

#### Illustration.

(1) In 1946, a parent company made a sale of plant to a subsidiary company.

The plant cost £10,000 in 1943, and wear and tear allowances had been made of—

1944-45 £1,200 ; 1945-46 £1,080 ; 1946-47 £1,012, total £3,292.

The sale price was £9,000 and the price it would have fetched in the open market £8,500. The limit of recharge is therefore the cost to the seller, £10,000, assuming no additions were made, and the open market value exceeds four-fifths of the limit of recharge. As no initial allowance was available to the seller, the buyer will not be entitled to one.

The capital expenditure still unallowed immediately before the sales is £10,000 - £3,292 = £6,708. The parties have therefore the option of taking this figure in lieu of the lower of open

market price or limit of recharge (the latter of which could, in the circumstances, have applied). In other words, the true written down value may be continued. If the option is not exercised, then there will be a balancing charge of £8,500 - £6,708 = £1,792 on the seller, and the buyer will get wear and tear allowances on the £8,500.

(2) If the above plant had been bought in 1946, and the sale taken place in 1949, the figures would have been—

Cost, 1946	.. .. .	£10,000
Initial Allowance 1947-48	..	£2,000
Wear & Tear Allowance 1947-48	1,250	
		<u>3,250</u>
		6,750
Wear and Tear Allowance 1948-49	..	<u>844</u>
		5,906
Wear and Tear Allowance 1949-50	..	<u>738</u>
		5,168
Still unallowed	.. .. .	<u>£5,168</u>

Sale price ignored.

Market Value	.. .. .	£8,500
Limit of recharge	.. .. .	£10,000
Four-fifths of limit of recharge	..	£8,000 (which is less than market value).
Substituted value	.. .. .	£5,168

The parties can either (a) proceed on the basis of the sale being at £8,500, in which case there will be a balancing charge on the seller of £8,500 - £5,168 = £3,332; and the buyer will get an initial allowance of £500 (the excess of the market value over four-fifths of the limit of recharge, being less than the initial allowance to the seller and the balancing charge on him), or (b) proceed on the written down value.

If there is a succession to a business on or after 6th April, 1946, so that the business is treated under Rule 11 as discontinued, any plant in use in the "old" business which continues to be used by the "new" one, will be treated as having been sold by the one to the other at the price it would have fetched if sold in the open market, but no initial allowance will be available to the successor.

If the business is carried on in partnership, the allowances are made to the partnership, notwithstanding changes (other than permanent discontinuance) in the partners (§ 60—I.T.A. 1945), *i.e.*, unless a claim is made under Rule 11 for the business to be regarded as discontinued (*see* § 68).

Where it is necessary for the purposes of the Income Tax Act, 1945, to apportion any sum (*e.g.*, on a lump sum purchase of a business), the apportionment will be agreed between the parties and the Inspector of Taxes. If there is a dispute, it will be determined—

- (a) if the same body of General Commissioners have jurisdiction over all the parties involved, by them, unless said parties agree to go to the Special Commissioners ;
- (b) if different General Commissioners are involved, by the General Commissioners directed by the C.I.R., unless the parties agree to go to the Special Commissioners ;
- (c) in any other case, by the Special Commissioners.

The same bodies determine any dispute as to the price plant would have fetched in the open market (§ 61—I.T.A. 1945).

A person must exclude from the cost price of plant any expenditure met directly or indirectly by the Crown, local authority or any other person, except for the purposes of a balancing charge on plant provided before 6th April, 1946. For this purpose, however, there can be left out of the disallowable costs, (a) any insurance or other compensation moneys payable in respect of any asset which has been demolished, destroyed or put out of use (this is to prevent double account being taken of such moneys, as they come in



as proceeds of sale); (b) any contribution by the Crown or local authority for which no allowance could be made under the next described relief.

Where on or after 6th April, 1946, a person, for the purposes of a trade carried on or to be carried on by him, or by a tenant of land in which he has an interest, contributes a capital sum to expenditure on the provision of plant, he is entitled to initial allowances and wear and tear allowances on his expenditure (as if he were the lessor if the contribution is to a tenant, *i.e.*, the burden of the wear and tear must fall on the contributor).

If, when the contribution was made, the trade was (or was to be) carried on by the contributor, and the trade is subsequently transferred, the wear and tear allowance for the year of assessment in which the transfer takes place, and all subsequent years, goes to the transferee. On transfer of part of a trade, the transferee gets the part of the allowance properly referable to the part transferred.

If the trade was carried on by a tenant, the wear and tear allowance is given to the person who, at the end of any year of assessment, is entitled to the contributor's interest in the land (§ 66 and 3rd Sch., I.T.A. 1945).

(The last two paragraphs do not apply to the occupation of woodlands; instead, the agricultural allowances apply.)

(e) *Exceptional Depreciation* (§ 19—1941; §§ 48-54— I.T.A. 1945; §§ 58, 59 and 8th Sch.—(No. 2) 1945; § 58—1946).

If buildings, machinery or plant have been provided since the beginning of 1937 for the purpose of the

business by the person carrying it on, and either (a) on 31st December, 1946, the value of the buildings, machinery or plant, or where the buildings, etc., have ceased to exist as such, the value of the remains thereof, is less than the net cost, or (b) the buildings, etc., are sold before that date for less than the net cost, and the deficiency is, in either case, wholly or mainly ascribable to conditions prevailing as a consequence of the war, a special allowance is provided. It is necessary to determine the net cost, *i.e.*, the capital outlay less any grants in aid by the Government or any other party, either towards the cost or towards wear and tear or obsolescence. Any sums provided by way of loan or under the War Damage Act, 1943, are *not* regarded as grants. From the net costs are deducted :

- (a) All deductions for wear and tear or depreciation already allowed (otherwise than under the present provision), *plus*
- (b) Any payments made or to be made under Part I or Part II of the War Damage Act, 1943, in respect of damage, other than damage made good before the relevant date or before the previous sale of the buildings, etc., as the case may be, where the assets have been sold before 31st December, 1946, or are no longer in existence as such, and the said payments have been or are to be made to or for the benefit of the person entitled to the allowance.

Where it is necessary to value buildings, plant, etc., on 31st December, 1946, the value is to be ascertained as if the assets were in a proper state of repair.

Pending an ascertainment whether an allowance falls to be made, the Commissioners of Inland Revenue, if satisfied that the assets are of such a nature that it is likely that a claim will ultimately arise, may make an interim allowance, not exceeding 10 per cent. of the net cost. The allowance is provisional and will be adjusted when the actual amount is ultimately ascertained.

If a trade is transferred, the successor gets the benefit of the allowance from the date of transfer, but the total allowance must not be more than if the transfer had not taken place.

Provision is made to prevent collusion where the buyer is controlled by the seller or the seller by the buyer, or both are controlled by a third party. In such a case, if the assets in question are sold on or before or not later than six years after 31st December, 1946, and the seller is the claimant of exceptional depreciation and at the time of the sale (and if the event giving rise to the allowance is not the sale, *also* at the time of the event), the assets are not in a proper state of repair, the buyer is not to be allowed any deduction for making good such disrepair, nor will he be entitled to wear and tear, etc., allowances on expenditure in making it good. This restriction cannot be avoided by a second sale to a controlled or controlling person.

The question of what, if any, exceptional depreciation allowance is to be given in respect of any asset(s) is determined by the C.I.R., who must give notice to the person entitled to the allowance, also of their decision as to—

- (a) how much of the price paid on the sale of two or more assets sold together is properly attributable to any of the assets; or

(b) what is the relevant price for any asset(s).

If any other persons are involved from the view-point of Income Tax liability, they must also give notice to him. The decision is subject to appeal to the Special Commissioners, and all the persons on whom notice is served are entitled to be heard.

All such adjustments, whether repayment or additional assessments, can be made as are requisite to ensure that the proper amounts of tax are paid after adding back any provisional allowances and giving the final allowances. The six years time limits do not apply.

#### Illustration.

A company built a factory in 1938 at a cost of £20,000, installing machinery costing £15,000. This machinery was worn out in 1941, and the scrap sold for £1,500 on 31st December, 1941, when machinery costing £32,000 was bought in its place. The factory was valued on 31st December, 1946, at £13,000, the plant at £9,000. Exceptional depreciation was granted; obsolescence allowance was not claimed on the replacement of the original plant. The Government contributed 25 per cent. of the cost of each asset.

		Factory.	First Plant.	Second Plant.
Cost	.. .. .	£20,000	£15,000	£32,000
Less Government grant	..	5,000	3,750	8,000
		<hr/>	<hr/>	<hr/>
Net cost	.. .. .	15,000	11,250	24,000
Sale price	.. .. .	—	1,500	—
Value, 31st December, 1946	..	13,000	—	9,000
		<hr/>	<hr/>	<hr/>
Exceptional depreciation	.. .. .	<u>£2,000</u>	<u>£9,750</u>	<u>£15,000</u>
Allowable 1939-40	.. .. .	£258	£3,545	—
1940-41	.. .. .	258	3,545	—
1941-42	.. .. .	258	2,660	£750
1942-43	.. .. .	258	—	3,000
1943-44	.. .. .	258	—	3,000
1944-45	.. .. .	258	—	3,000
1945-46	.. .. .	258	—	3,000
1946-47	.. .. .	194	—	2,250

Any wear and tear or other depreciation allowances given must be deducted.

Any amount allowed under these provisions ranks as wear and tear allowance for all purposes of the Acts.

By concession, where buildings, etc., provided since the beginning of 1937, are employed side by side with older buildings, etc., and either old or new become redundant, the Revenue will entertain a claim by reference to the net cost and deficiency of value of the new buildings, etc. Relief is given under the section for air-raid shelters used exclusively as such, and the cost of demolishing them will in due course be added to the cost for this purpose.

### § 5.—Deduction in respect of Property.

#### (a) *Rent or Net Annual Value.*

The rent of premises used solely for purposes of business, and not as a place of residence, can be charged as a business expense. Where no rent is paid, the net annual value of such premises may be charged in lieu of rent.

This is necessary in order to avoid a double assessment. A tenant really pays over to his landlord part of his profits when he pays rent, and is only liable to return as his own profits what is left. An owner-occupier must be placed in the same position ; he pays income tax under Schedule A on the annual value of the premises, and to that extent, has paid tax on the profits. He is therefore allowed to deduct the net annual value in arriving at his profits for the purposes of Schedule D.

Likewise, where a tenant is paying a rent which is less than the net annual value, he is in the position of a landlord so far as the beneficial occupation is concerned. He is therefore entitled to deduct the excess

of the net annual value over the rent, in addition to the rent itself. In other words, there can always be deducted the rent paid or the net annual value, whichever is the higher.

### Illustration (1).

The following is the Profit and Loss Account of George Barnes for the year ended 31st March, 1947. The trade premises are held on lease, at a rent of £160 per annum. Show the Schedule D assessment for 1947-48. The premises are assessed under Schedule A at £200 net.

PROFIT AND LOSS ACCOUNT				
Dr.	For the year ended 31st March, 1947.			Cr.
		£		£
To Trade Expenses .. ..	..	155	By Gross Profit from Trading Account	1,138
„ Salaries .. ..	..	195		
„ Rent .. ..	..	160		
„ Income Tax, Sch. D .. ..	..	22		
„ Income Tax, Sch. A .. ..	..	18		
„ Bad Debts .. ..	..	81		
„ Interest on Capital .. ..	..	50		
„ Net Profit .. ..	..	457		
		£ 1,138		£ 1,138

### INCOME TAX COMPUTATION.

Net Profit as per Accounts .. ..	£457
Add Rent .. ..	160
Income Tax, Sch. D .. ..	22
Income Tax, Sch. A .. ..	18
Interest on Capital .. ..	50
	<u>707</u>
Deduct Schedule A Net Annual Value ..	200
	<u>£507</u>
Assessable Profit .. ..	
Assessment 1947-48 .. ..	<u>£507</u>

### Notes to Illustration.

- (1) RENT.—Where the Net Annual Value is charged in lieu of rent, the actual rent paid should be written back and the Net Annual Value deducted. This method is clearer than merely deducting the difference between the two figures.

(2) INCOME TAX UNDER SCHEDULE A.—Income Tax is one and the same tax, whether it is collected under Schedules A, B, C, D or E. It is regarded as an appropriation of profits, and therefore cannot be charged. The above item represents the proportion of the tax, in respect of the premises, which the occupier is not able to recoup from the landlord. Tax at 9/- in the £ for 1946-47, paid during the year was on £200, amounting to £90. The actual rent paid amounted to £160, and in consequence, the occupier could not deduct more than 9/- in the £ on that amount, viz., £72. The balance of £18 represents the proportion of tax which he himself has borne.

The excess of the Net Annual Value (£200) over the rent paid (£160), i.e., £40, measures the tenant's beneficial occupation of the premises, and that amount must be included as part of his Statutory Total Income, against which he is entitled to the appropriate personal and similar allowances. In arriving at the tax payable by him, he is, of course, credited with having paid the tax thereon.

The transactions will show in the books of the business as follows:—

Dr.		RENT ACCOUNT.				Cr.			
1946.		£	s.	d.	1947.		£	s.	d.
Apl. 1	To Balance b/f. tax deductible from June rent	40	0	0	Mar. 31	By Profit and Loss Account	160	0	0
Sept. 20	„ Cash—Rent .. ..	40	0	0		„ Balance, tax deductible from rent payable on 24th June c/d. ..	32	0	0
Dec. 25	„ Cash—Rent .. ..	40	0	0					
1947.									
Mar. 31	„ Sch. A tax chargeable to Landlord 9/- in £ on £160 Rent paid.. ..	72	0	0					
		<u>£192 0 0</u>					<u>£192 0 0</u>		
1947.									
Apl. 1	To Balance b/d. .. ..	32	0	0					

Dr.		SCHEDULE A TAX ACCOUNT.				Cr.			
		£	s.	d.			£	s.	d.
1946.					1946.				
Apl. 1	To Cash .. ..	40	0	0	Apl. 1	By Balance b/d. ..	40	0	0
1947.					1947.				
Jan. 1	" Cash—				Mar. 31	By Rent Account—			
	Sch. A tax, 9/- in £					Sch. A tax chargeable			
	on £200 = £90 0 0					to Landlord, 9/- in £			
	Less Excess of					on £160 Rent, being			
	tax deductible					less than Net Annual			
	from rent over					Value .. ..	72	0	0
	next payment	82	0	0					
			58	0	0				
Mar. 31	.. Balance c/d. ..	32	0	0		.. Profit and Loss Account	18	0	0
			£180	0	0				£180 0 0
1947.					1947.				
Apl. 1	To Cash .. ..	32	0	0	Apl. 1	By Balance b/d. .. ..	32	0	0

The tax deductible from the landlord in excess of the next payment of rent is arrived at as follows :—

		1945/46		1946/47
Tax on rent of £160	@ 10/-	80	@ 9/-	72
Quarter's rent		40		40
		<u>£40</u>		<u>£32</u>
Sch. A tax on £200	@ 10/-	100	@ 9/-	90
Excess deferred		40		32
		<u>£60</u>		<u>£58</u>
Payable 1st January				

In practice, the payment of tax is now usually made in time to deduct immediately, *i.e.*, tax due on 1st January is paid early enough to be deducted from the December rent.

Where a business occupies a number of leasehold warehouses for the purposes of its trade, and closes down one of them for motives of economy, the lease rent of that warehouse (subject to adjustment of rents received from sub-tenants) is still a proper deduction in the accounts, being laid out exclusively for the purpose of trade (*C.I.R. v. Falkirk Iron Co.* (1933), 17 T.C. 625). A similar result follows where a branch shop is closed on the grounds that the business done there is unprofitable and is sublet at a loss (*Hyett v. Lennard* (1940), T.R. 279). (Rent paid under a *long* lease will not be deductible, as tax is deductible at source from such rent.)

In the case of a business, *e.g.*, a bank, which owns the buildings in which the business is carried on, and portions of the buildings are occupied as residences by managers and agents, the annual value of the whole premises may be deducted in arriving at the liability to assessment (*Russell v. Aberdeen Town and County Bank* (1888), 2 T.C. 321).

In the case of premises abroad used for business purposes, the rent paid is an admissible deduction, even if it is dependent on the amount of profits (*Union Cold Storage Co. v. Adamson* (1931), 16 T.C. 293).



In the case of properties situated in this country, Section 24 (1) of the Rating and Valuation Act, 1925 (*see* Appendix IV), took out of rating the machinery specified, this being broadly process machinery. Schedule A assessments on factories also exclude process plant; non-rateable machinery is not to be taken into account in ascertaining the annual value of any property for the purposes of Schedule A, or for the purposes of the depreciation allowance of factories (§ 22—1936).

It is not uncommon for an owner-occupier of business premises to charge in the Profit and Loss Account a hypothetical amount in lieu of rent, based possibly on a percentage of the estimated value of the premises. Any amount so charged must be written back, and the net annual value for Schedule A charged in lieu thereof. Where one of the partners in a firm owns the premises where the business is carried on, the rent *bond fide* paid to him for the premises is a proper debit in the firm's accounts; the rent is received by the partner in his character of landlord (*Heastie v. Veitch & Co.* (1933), 18 T.C. 305).

Prior to 1940-41, the Sch. A assessment exhausted the taxable capacity of the property in land and buildings, and if the land or buildings were let at a profit rental, the difference between the rent receivable and the annual value was not taxable. Any profit derived from the provision of services was chargeable to tax under Sch. D as a business, but the profits from letting *simpliciter* were covered by the Sch. A assessments, and no assessment could be raised on the excess of the rent received over the Net Annual Value (*Salisbury House Estate v. Fry* (1930), 15 T.C. 266). If, however, premises were let *furnished*, the profits thereon were assessable under Case VI, Sch. D. For 1940-41 onwards, all profit rentals are assessable (*see* Chap. III, § 1 (g)), whether the letting is furnished or unfurnished.

Where only part of the premises was sublet, the rent receivable credited to Profit and Loss Account was deducted from profit, and the proportion, applicable to the portion sublet, of the charges for rent or annual value (whichever was charged), and for any other expenses covered by the rent receivable, *e.g.*, rates, lighting, etc., was written back.

### Illustration (2).

The following is the Profit and Loss Account of M, who sublets one-fourth of his business premises at a rent including rates, lighting and heating. The Net Annual Value of the whole premises is £200.

PROFIT AND LOSS ACCOUNT					
Dr.		For the Year ended 31st December, 1938.		Cr	
		£			£
To Rent .. .. .	180	By Gross Profit .. .. .	1,226		
„ Rates .. .. .	100	„ Rent Receivable .. .. .	100		
„ Lighting and Heating .. .. .	60				
„ General Expenses .. .. .	000				
„ Mortgage Interest .. .. .	20				
„ Repairs to Premises .. .. .	16				
„ Depreciation .. .. .	50				
„ Net Profit .. .. .	800				
	<u>£1,326</u>				<u>£1,326</u>

### INCOME TAX COMPUTATION.

Net Profit per Profit and Loss Account	£	300
<i>Add</i> Rent .. .. .	180	
Rates ( $\frac{1}{4}$ ) .. .. .	25	
Lighting and Heating ( $\frac{1}{4}$ ) .. .. .	15	
Mortgage Interest .. .. .	20	
Repairs ( $\frac{1}{4}$ ) .. .. .	4	
Depreciation .. .. .	50	
	<u>594</u>	
<i>Deduct:</i>		
Rent Receivable .. .. .	£100	
Net Annual Value .. .. .	£200	
Less Proportion applicable to premises sublet ( $\frac{1}{4}$ ) .. .. .	50	
	<u>150</u>	
		<u>250</u>
Adjusted Profit		<u>£344</u>

*Note to Illustration.*

Since only three-fourths of the business premises were used for the purpose of the business, only three-fourths of the Net Annual Value, rates, lighting and heating and repairs were allowed as a deduction in arriving at the business profits for assessment, and the remaining quarter of such expenses was therefore written back. It may have been the fact that the repairs, etc., applicable to the premises sublet represented some other fraction of the whole; if so, the amount in fact spent on the sublet premises would have been written back. The whole of the rent received on the part sublet was eliminated from the profit, as tax under Schedule A had been paid on the Net Annual Value of the whole of the premises, and the profit rental was not assessable.

Where the annual value of the portion sublet could not be conveniently ascertained, the rent receivable was left in charge, and the whole annual value, etc., deducted. This course is now the most convenient one to adopt rather than to take out profit rentals for separate assessment.

If part of the premises is used for private purposes, *e.g.*, where the occupier lives over his shop, only a fair proportion of the rent or annual value must be allowed in respect of the part of the premises used for the business. The proportion of the rent or net annual value to be disallowed is generally one-third, but is adjusted to meet the facts; *e.g.*, one-third would obviously be excessive in the case of an hotel. In such cases, due adjustment must also be made for a proportion of rates, insurance, lighting, heating, etc., applicable to the part privately occupied.

It may be that the Schedule A assessment is altered during an accounting year. Where this happens and the net annual value is allowable as a deduction in the accounts, it is necessary to apportion the assessments according to the period of the accounts of the year of the change. (N.B.—No adjustment of the

*assessment based on the previous year's accounts is permissible in the year of assessment in which the change occurs.)*

**Illustration.**

A business makes up its accounts to 31st December. For 1945-46 the Net Annual Value of the premises owned was £400, and for 1946-47 it was £450. In the accounts to 31st December, 1946, there will be charged  $\frac{1}{12}$ ths of £400 +  $\frac{11}{12}$ ths of £450 = £438.

*(b) Depreciation, etc.*

(i) Position up to 5th April, 1946.

In the case of MILLS, FACTORIES AND OTHER SIMILAR PREMISES owned by the person carrying on the trade, and occupied by him for the purposes of the trade, an additional allowance is made for DEPRECIATION of the premises (§ 15—1937). For this purpose, a tenant is treated as owner only if, under the lease or tenancy agreement, the whole burden of any depreciation of the premises falls upon him. A repairing lease containing a strict covenant for repair does not comply with this requirement (*Boarland v. Pirie Appleton & Co.* (1940), T.R. 107). In practice, the buildings in respect of which the allowance is granted are buildings of the character of mills and factories, containing machinery moved or worked by steam, water or other mechanical power, together with buildings such as stores, warehouses or administrative offices which are ancillary to and form part of the mill or factory premises.

The allowance, which is a deduction from the profits, is as follows :—

- (1) Premises assessed under Schedule A (other than electricity works or brickworks):

The lower of these two amounts—

- (a) The repairs allowance for Schedule A, or
- (b) (i) If the premises are in London or Scotland, one-sixth of the *gross* annual value for rating purposes ;  
(ii) If the premises are elsewhere in England, one-fifth of the net annual value for rating purposes.

Where rooms, etc., used for air raid protection only are exempted from Schedule A tax, the repairs allowance on the notional Schedule A value is allowed to be added to the above allowance (§ 17—1938).

(2) Premises consisting of or comprising electricity works or brickworks and premises not assessed under Schedule A (*e.g.*, factories, etc., abroad) :

An amount equal to one per cent. of the cost of the building (including the site), provided that the building contains, and is used wholly or mainly for the purpose of operating machinery worked by steam, electricity or other mechanical power ; or the depreciation of the building is substantially increased by the operation therein of such machinery. Non-rateable machinery is ignored.

In accounts for less or more than a year, the allowances are apportioned. The allowance for depreciation is in addition to the net annual value in the case of premises assessed under Schedule A. In other cases there is no annual value to deduct.

In accounts forming the basis of assessment for years prior to 1937-38, a similar allowance was granted in effect by allowing the gross annual value to be deducted instead of the net annual value (Rule 5, Cases I and II). Where the premises were situate outside the United Kingdom, a sum equal to one-sixth of the estimated annual value could be deducted if the occupier was the owner (§ 18—1919). This did not rank as a “ Mills, factories, etc.” allowance, however. (*See* Chap. IV, § 3 (b) *re* exceptional depreciation during the war.)

(ii) Position from 6th April, 1946.

(a) As from 6th April, 1946, initial and annual allowances are given on any new industrial buildings

or any new capital expenditure incurred on existing industrial buildings since 6th April, 1944. Annual allowances are also given on such buildings where the capital expenditure was incurred within 50 years prior to 6th April, 1946.

The definition of buildings ranking for allowance is much wider than that of buildings hitherto attracting the mills, factories, etc., allowance, being as follows :—

The expression “ industrial building or structure ” means a building or structure in use—

- (a) for the purposes of a trade carried on in a mill, factory or other similar premises ; or
- (b) for the purposes of a transport, dock, inland navigation, water, electricity or hydraulic power undertaking ; or
- (c) for the purposes of a trade which consists in the manufacture of goods or materials or the subjection of goods or materials to any process ; or
- (d) for the purposes of a trade which consists in the storage—

(i) of goods or materials which are to be used in the manufacture of other goods or materials ; or

(ii) of goods or materials which are to be subjected, in the course of a trade, to any process ; or

(iii) of goods or materials which, having been manufactured or produced or subjected, in the course of a trade, to any process, have not yet been delivered to any purchaser ; or

(iv) of goods or materials on their arrival by sea or air into any part of the United Kingdom ;  
or

- (e) for the purposes of a trade which consists in the working of any mine, oil well or other source of mineral deposits, or of a foreign plantation ; or
- (f) for the purposes of a trade consisting in all or any of the following activities, *i.e.*, ploughing or cultivating land (other than land in the occupation of the person carrying on the trade) or doing any other agricultural operation on such land, or threshing the crops of another person.

A building or structure provided for the welfare of employees and so used, is included (§ 8—I.T.A. 1945).

(Reference to a building, etc., includes a reference to a part of a building (§ 68—I.T.A. 1945.))

Where a building is in use for part only of a trade, the above definition applies, but if part only of a trade complies with the definition, the building must be in use for that part of the trade.

The following are not included : Any building or structure in use as, or as part of, a dwelling house, retail shop, showroom, hotel or office or for any purpose ancillary to the purposes of a dwelling house, retail shop, etc. (*See (c) below as to mines, etc.*)

If part of a building is not within the definition, and the capital expenditure on that part is not more than one-tenth of the capital expenditure on the whole, the whole building will be treated as within the definition ; otherwise the expenditure on the part must be excluded.

The allowances are given in the year of assessment in the basis period for which the expenditure was incurred, in the same way as already explained for Wear and Tear, etc. (§ 6—I.T.A. 1945). (*See Chap. IV, § 3.*)

(b) *Capital Expenditure incurred on or after 6th April, 1946.*

An initial allowance of 10 per cent. of the capital expenditure, and an annual allowance of 2 per cent. for 45 years, writes off the cost over 45 years (§§ 1, 2—I.T.A. 1945).

(c) *Capital Expenditure incurred after 5th April, 1944, but before 6th April, 1946.*

The amount expended, less any sums already allowed by way of mills, factories, etc., allowance or exceptional depreciation allowance, will attract initial allowance as if the expenditure had been incurred on 6th April, 1946 ; and an annual allowance will be given of 2 per cent. of the cost, until the cost of the asset is written off by allowances (*i.e.*, the mills, etc., allowances, initial and annual allowances cannot exceed the original cost) (§§ 1, 2—I.T.A. 1945).

(d) *Capital Expenditure incurred within 50 years before 6th April, 1946.*

Unless the expenditure was incurred after 5th April, 1944, there will be no initial allowance, but the annual allowance of 2 per cent. of the expenditure will be given until the 50 years from the date on which the expenditure was incurred expires (§ 2—I.T.A. 1945).

(e) In no case can an allowance be given after the fiftieth year following that in which the building was first used.

If an industrial building is scrapped, sold or destroyed within the fifty years, there will be a balancing allowance or balancing charge, as explained later. In general, allowances continue to be calculated by reference to the cost to the original owner ; if a new owner pays more, he gets no allowance on the excess.



(f) The new allowances displace the mills, factories, etc., allowances for all buildings constructed after 5th April, 1946, but if a trader was getting the mills, etc., allowance for 1945-46 (*i.e.*, by a charge in the computation of profit for that year of assessment) on any building, this allowance will continue for that building for five years from 6th April, 1946, and the operation of the 1945 Act will be accordingly postponed in respect of that building. At any time within those five years, however, he may give notice that he wants to go on to the new Act, in which case the new Act will apply for the year of assessment in which the notice is given and for all future years. It may pay not to give the notice where rateable machinery is included in the annual value of the property, so that the mills allowance exceeds the annual allowance (§ 7—I.T.A. 1945).

Buildings which rank for the scientific research allowance do not, of course, attract relief under the industrial building provisions.

The term "structure" includes artificial works such as walls, bridges, dams, roads, dry docks and linings.

Relief is not given on capital expenditure incurred on the acquisition of, or rights in or over, any land, or on preparing, cutting, tunnelling or levelling any land. The expense of work done on the land for the purpose of preparing it to receive the foundations of the building or structure, being work that will be valueless when the building, etc., is demolished, and not work consisting of cutting or tunnelling, however, ranks for relief (§ 14 (1)—I.T.A. 1945).

A building is only eligible for allowances while it is in use as an industrial building; if it is transferred to

a trade not covered by the definition, allowances cease. Temporary disuse, however, is no bar to allowances (§ 11—I.T.A. 1945).

*(g) Persons who may claim.*

The initial allowance goes to the person who incurs the expenditure on the construction of the building, provided he is either the owner or the lessee of the land on which it is built and he builds it for use in his own business or in that of a trading tenant or sub-tenant. A person who buys a new building before it has been used, however, is entitled to the allowance if the building is for the use of his own or a tenant's trade (§ 1—I.T.A. 1945).

The annual allowance goes with the "relevant interest" in the building, *i.e.*, the interest in the building to which the person who incurred the expenditure was entitled when he incurred it. (*See* § 10—I.T.A. 1945, where two or more persons are interested, etc.) A successor to the "relevant interest" succeeds to the right to the allowance. No allowances are due to any one merely renting a building, even if he has paid a premium for the lease, unless he has incurred capital expenditure on the building or acquired the relevant interest of the person who incurred such expenditure.

*(h) Expenditure eligible.*

Capital expenditure qualifies for the allowances if incurred on the construction, reconstruction or alteration or additions to industrial buildings (as distinct from the land—see above), unless the expenditure qualifies for allowances for mining, agriculture or scientific research. It is only expenditure that cannot be allowed in computing profits that qualifies. Con-

tributions from the Crown or local authorities must be deducted from the expenditure. A contribution from any other person, however, is different. If the contribution is for the purposes of a trade carried on by the contributor or by his tenant, the contributor is entitled to allowances on his expenditure; and the person who provided the building to allowances on his own net expenditure. In any other case the contribution is not deductible and allowances will be made on the full expenditure (§ 66—I.T.A. 1945).

If a person buys an industrial building before it is used, he gets allowances on what he pays for it, so long as that sum does not exceed the cost of construction. If he buys it from a builder, unused, he gets allowances on the cost to him (§ 5—I.T.A. 1945).

#### Illustration.

Cost of factory .. .. .	£30,000
Less Contribution by Crown .. ..	5,000
	<hr/>
	25,000
Contribution by landlord .. ..	10,000
	<hr/>
Cost to tenant .. .. .	<u>£15,000</u>

The landlord is entitled to allowances on £10,000, the tenant on £15,000. If, however, the £10,000 had been contributed by anyone else, other than a public or local authority, the tenant would be entitled to allowances on £25,000, the contributor to none.

#### (i) *Initial allowances* (§ 1—I.T.A. 1945).

It is emphasised that the initial allowance is given only once in respect of the same building, and not, as is the case with plant and machinery, to each person who buys the asset. It is given to the person who incurs the expenditure, as explained above, in the year of assessment for which the year in which the

expenditure is payable forms the basis period. If, however, the building is erected and then let before it is used, the allowance is related to the basis period in which the tenancy begins (§§ 1, 64 (2)—I.T.A. 1945). If a lessor is entitled to the allowance, the actual expenditure in the year of assessment itself forms the basis of the allowance for that year of assessment.

Where the capital expenditure is incurred prior to commencing business, it is treated as incurred on the day the business commenced.

**Illustration (1).**

A manufacturer making up accounts to 31st January, built a new wing on his factory for which he had to pay on 1st September, 1946, £12,000, and on 1st March, 1947, £8,000. The £12,000, is in the basis period for 1947-48 (accounting year to 31st January, 1947); the £8,000 in the basis period for 1948-49. (Special rules apply to new businesses as already explained in connection with plant.) The initial allowances are therefore: 1947-48, £1,200; 1948-49, £800, given in the same way as wear and tear allowances.

Capital expenditure incurred on or after 6th April, 1944, but before 6th April, 1946, attracts the initial allowance on the cost less any allowances given for 1944-45 and 1945-46 for mills, factories or exceptional depreciation. (Where relevant, the mills, factories, allowance must be apportioned over the buildings to which it relates (§ 65 (3)—I.T.A. 1945).) If the mills and factories allowance is allowed to continue for the five years to 5th April, 1951, the initial allowance will, of course, be given on the cost less all allowances up to that date.

No initial allowance will be given where the building has been sold, demolished or destroyed before 6th April, 1946, or where it is no longer an industrial building on that date, or was erected by a lessee whose leasehold interest has ended before that date (unless the lessee acquired the reversion).

**Illustration (2).**

Building erected in 1944, payments being due as follows :—  
1st May, 1944, £10,000 ; 1st November, 1944, £12,000.

Company's accounts made up to 30th September in each year. Mills, factories, etc., allowance granted in accounts :—

Year to 30th September, 1944, £20.

Year to 30th September, 1945, £105.

As the allowance charged in the accounts for the year to 30th September, 1945, would in fact give relief in 1946-47, it must be disallowed (§ 55 (4)—I.T.A. 1945), otherwise there would be an overlap with the annual allowance.

The initial allowance would therefore be calculated on £22,000 — £20 = £21,980, 10 per cent. of which is £2,198, which would be given in 1947-48, since the expenditure is *deemed* to have been made on 6th April, 1946, which is in the basis period (year to 30th September, 1946) for the year of assessment 1947-48. Notice would be given of the election to discontinue the mills, factories, etc., allowance.

In deciding whether or not to make such an election, it must be borne in mind that if the Mills and Factories allowance is continued until 6th April, 1951, the Initial Allowance, which would be given in 1952-53, will be reduced by 10% of the total of the allowances given from 1946-47 to 1950-51. The result may be that even though the Mills and Factories Allowance exceeded 2% of the expenditure, it may still be advantageous to discontinue it at 6th April, 1946.

*(j) Residue of Expenditure (§ 4—I.T.A. 1945).*

This is what accountants would call the "written down value" of the building, *i.e.*, the original capital expenditure, less—

- (i) Any initial, annual or scientific research allowances made ;
- (ii) A notional deduction (equal to the annual allowance otherwise applicable) for any year of assessment (after that in which the building was first used), for which it does not qualify for an annual or scientific research allowance (*e.g.*, because of a period of non-industrial user

or because the year in question was before 1946-47).

- (iii) Any excess of the mills, factories, etc., and exceptional depreciation allowances over the notional annual allowances up to and including the year of assessment ending on the day preceding the appointed day.

If any exceptional depreciation allowance is made for the year of assessment in which the appointed day falls, an amount equal to that allowance must be written off as at the end of the immediately preceding year of assessment (§ 26—1947). (*See (f)* above as to the postponement of the appointed day.)

- (iv) Any balancing allowance on sale ; and plus—  
(v) Any balancing charge on sale.

**Illustration (1).**

Capital expenditure, 1946 .. .. .	£10,000
Initial allowance, 1947-48 .. .. .	£1,000
Annual allowances, 1947-48 to 1951-52 ..	1,000
Notional allowances, 1952-53 and 1953-54, when not used as industrial building	400
Annual allowances, 1954-55 to 1957-58 ..	800
	<hr/> 3,200
	<hr/> 6,800
Balancing allowance, 1958-59 .. .. .	450
	<hr/> £6,350
Residue of expenditure .. .. .	<u>£6,350</u>

- (*k*) *Annual allowance* (§ 2—I.T.A. 1945).

To qualify for an annual allowance, the building must have been in industrial use on the last day of the basis period for the year of assessment for which the allowance is claimed, or temporarily disused on that date, following industrial user. The annual allowance ceases when the residue of expenditure is reduced to nil.

The annual allowance is 2 per cent. of the original capital expenditure on the construction of the building (excluding the cost of the land), except where the building has been sold, when it is computed on the residue of the expenditure immediately after the sale (see (1)). If the building was in existence on 6th April, 1946, the annual allowances from 1946-47 are 2 per cent. on the original capital expenditure on construction, but are limited in the aggregate to the residue of expenditure after deducting notional allowances for all years to 5th April, 1946. In no case, therefore, can allowances continue beyond the 50th year from the date of first user.

#### Illustration (2).

A manufacturer making up his accounts to 31st December, spent £20,000 on factory extensions in 1947, the original factory having been completed and used in 1935. The mills, factories, etc., allowance was less than 2 per cent. of the cost of the factory buildings, £30,000.

Cost of factory, 1935	.. .. .	£30,000
Notional Allowances, 1936-37 to 1945-46 at 2% per annum	.. .. .	6,000
		<hr/>
Residue of expenditure 6th April, 1946		<u>£24,000</u>
Annual allowance thereafter	.. .. .	£600
Cost of extensions, 1947	.. .. .	£20,000
Initial allowance thereon, 1948-49	.. .. .	£2,000
Annual allowance on extensions, 1948-49 and thereafter	.. .. .	£400
Total Annual Allowance, 1948-49 onwards	.. .. .	£1,000

#### (1) *Buildings sold after 5th April, 1946.*

On the sale of a building, the buyer gets no initial allowance. His annual allowance is based on the residue of the expenditure immediately after the sale, and is calculated by dividing such residue by the

number of years of assessment, up to and including the fiftieth year after the year in which the building was first used.

### Illustration.

Building cost £14,000 in 1948, sold in October, 1958, to another trader. All accounts are made up to 31st December.

Cost	£14,000
Initial Allowance, 1949-50	£1,400
Annual allowances, 1949-50—1958-59	2,800
	<hr/> 4,200
Residue before Sale	9,800
Excess of residue before sale over sale price (balancing allowance to seller)	1,200
Residue after sale	<hr/> <u>£8,600</u>

The buyer will be entitled to annual allowances until 1998-1999, *i.e.*, for 40 years, of one-fortieth of £8,600 or £215 per annum, commencing in 1959-60.

(For the effect of notional allowances, see (m).)

### (m) *Balancing Allowances and Balancing Charges* (§ 3—I.T.A. 1945).

On or after 6th April, 1946, wherever a building, while in use (or *temporary* disuse) as an industrial building, is sold, destroyed or scrapped (permanently put out of use), or the relevant interest on it is lost on the termination of the lease or of a foreign concession, a balancing allowance is available if the proceeds are less than the residue of the expenditure before sale, while a balancing charge will be made if the proceeds exceed that residue.

Proceeds include the amount realised by the sale, or any proceeds of insurance, salvage or compensation.

No allowance or charge can be made if the sale, etc., is later than the end of the basis period for the



fiftieth year of assessment after the first user of the building.

A balancing charge cannot exceed the allowances which the taxpayer has actually received by way of mills, factories, etc., exceptional depreciation, scientific research allowances, and any allowances under the Income Tax Act, 1945, *i.e.*, it can only take away the total of any allowances already made, but cannot charge tax on a profit over and above that figure, or on notional allowances.

If for any relevant years of assessment (*i.e.*, all years from the year of first user or from the date of the last sale while in industrial use), a notional allowance has to be written off, a balancing allowance will still be made on the excess of the residue over the proceeds, but a balancing charge will be reduced by a fraction whose numerator is the number of relevant years for which an annual allowance or scientific research allowance has been made, and the denominator the total of the relevant years (§ 3 (4)—I.T.A. 1945; § 33—I.T.A. 1946). (The taxpayer can claim the fractional method for the balancing allowance if he so desires.)

Where there is a balancing allowance to the seller, the buyer's "residue of expenditure after the sale" is the residue before the sale less the excess of that residue over the proceeds, *i.e.*, normally what the buyer pays for the asset. If, however, there is a balancing charge, the residue before the sale is increased by the amount on which that charge is made (which may be a fraction of the excess of the proceeds over the residue before sale—*see* above) (§ 4—I.T.A. 1945).

**Illustration.**

Building costing £10,000, first used in 1935 ; no mills, factories etc., allowance. Sold in 1965 for £5,500.

Cost 1935 .. .. .	£10,000
Notional allowances, 1936-37 to 1945-46	2,000
Annual allowances, 1946-47 to 1965-66	4,000
	<hr/> 6,000
Residue before sale .. .. .	4,000
Sale proceeds .. .. .	5,500
Residue as above .. .. .	4,000
	<hr/> £1,500

Balancing charge restricted to the fraction—

No. of years for which allowances given	20	
	<hr/>	$\times 1,500$
No. of relevant years	30	1,000

Residue after sale .. .. .	<hr/> £5,000
----------------------------	--------------

The purchaser is entitled to annual allowances for 20 years, *i.e.*, 1/20th of £5,000 = £250 per annum.

Thus the purchaser does not get his full purchase price allowed.

The purchaser keeps the building for a further 10 years (till 1975), during two of which it was not used as an industrial building, selling it while so used for £2,000.

Residue of expenditure after sale to him	£5,000
Less Annual allowances, 8 years at £250 .. .. .	£2,000
Notional allowances, 2 years at £250 .. .. .	500
	<hr/> 2,500
Residue before sale by him .. .. .	2,500
Proceeds .. .. .	2,000
	<hr/> £500

He would hardly claim to have the fraction (8/10ths) applied to this.

The new owner will be entitled to an annual allowance for 10 years of 1/10th of £2,000 = £200.

(n) *Lessors.*

Where a lessor is entitled to allowances under the Act, relief is given primarily against income from industrial buildings in the same year, *i.e.*, his basis period is the same as the year of assessment, but he can claim, within 12 months after the end of the year of assessment to have it set against other income of the same year. A balancing charge is made under Case VI of Sch. D (§ 56—I.T.A. 1945).

(o) *New business, etc.*

**Illustrations.**

(1) New business set up on 6th April, 1946, making up accounts to 5th April, 1947. The first accounts form the basis of assessment for 1946-47 and 1947-48, but for the purposes of the Income Tax Act, 1945, will be regarded as the basis period for 1946-47 only.

(2) Accounts made up regularly year by year until 30th September, 1946, then an 18 months account to 31st March, 1948, and yearly thereafter to 31st March.

Basis period for 1947-48: Year to 30th September, 1946.

Basis period for 1948-49: 12 months to 31st March, 1948.

The six months to 31st March, 1947, will be regarded as part of the basis period for 1948-49, *i.e.*, expenditure during that six months will be added to that for the year to 31st March, 1948.

(p) *Anti-avoidance provisions.*

The provisions of § 59—I.T.A. 1945, already explained in connection with sales of plant, etc., apply, with modifications to sales of industrial buildings. If the sale is between persons under a common control or is regarded as having the main object of obtaining an allowance under the Act, the open market value is to be taken as the sale price, and allowances to seller and buyer calculated accordingly. If the case is one of common control only, however, the parties may elect that the sale be regarded as having taken place at the residue of expenditure

before the sale, unless that is more than the open market price. If the "residue" method is adopted, and the buyer subsequently sells or scraps the building, any balancing charge then due will be calculated as if the seller had continued to own the property, any sums provisionally allowed for exceptional depreciation being left out of account.

### Illustration.

Building cost £20,000 in 1946, sold in 1948 by parent company to subsidiary for £15,000, when the open market value was £19,000.

Cost, 1946	.. .. .	£20,000
Initial allowance 1947-48	.. .. .	£2,000
Annual allowances, 1947-48—1948-49	800	
		<u>2,800</u>
Residue before sale	.. .. .	<u>£17,200</u>

Assuming that it is agreed that the object is not to obtain allowances under the Act, the sale can be treated as at (a) £19,000 or at (b) £17,200.

Comparision	(a)	(b)
Residue before sale	.. £17,200	£17,200
"Sale price"	.. 19,000	17,200
	<u>£1,800</u>	<u>Nil.</u>
Balancing charge on vendor		
Residue after sale	.. £19,000	£17,200
Annual allowances to buyer		
1/48th	.. £396	£358

If the buyer retains the building for 20 years during which it was in industrial use, when it was sold for £18,000 :

Residue as above	.. £19,000	£17,200
20 Annual allowances	.. 7,920	7,160
	<u>11,080</u>	<u>10,040</u>
Proceeds	.. 18,000	18,000
	<u>£6,920</u>	<u>£7,960</u>
Balancing charge	.. .. .	

In (b) although the proceeds exceed the cost to the buyer, the balancing charge will not be restricted to the allowances made to the buyer, but must be calculated as if the original seller still owned the building; i.e., it does not exceed the total of the allowances given to the seller *and* the buyer.

(q) *Apportionment of consideration.*

The same rules apply as already described in the case of plant, etc. (§§ 58, 161—I.T.A. 1945). (See § 4 of this Chapter.)

(r) *Successions.*

Here again, the rules are the same as in the case of plant (§ 60—I.T.A. 1945). (See § 4 of this Chapter.)

### § 6.—Interest on Loans and other Annual Payments.

Since the Income Tax is collected from the person paying annual interest, who reimburses himself by deducting Income Tax from the interest when he pays it, annual interest is not allowed as a deduction in arriving at the profits of a trade or business.

Interest other than annual interest, *e.g.*, interest on short loans from bankers and others, is payable without deduction of tax and is allowed as an expense, the assessment being made upon the recipient. Where the recipient is non-resident and has no agent here, no assessment is made.

Interest paid on temporary loans is allowable as expenditure by means of which the company procure the use of the thing by which they make a profit (*Scottish North American Trust Ltd. v. Farmer* (1912), A.C. 118).

Interest on large advances to finance hire purchase transactions, however, is in the nature of interest on fixed working capital, as distinct from temporary accommodation, and, whether short or annual interest, is expenditure in respect of capital and consequently not an admissible expense for purposes of Income Tax (*The European Investment Trust Co. Ltd. v. Jackson* (1932), 18 T.C. 1).

#### (a) Deduction of Tax—General Rules 19 and 21.

The deduction of tax from annual payments is authorised by General Rules 19 and 21. If the payment

is made out of income charged to tax, General Rule 19 applies ; if the payment is made otherwise, *e.g.*, out of capital, General Rule 21 directs deduction of tax.

Under General Rule 19, it is provided that in respect of all annuities, yearly interest of money, or other ANNUAL PAYMENTS, PAYABLE OUT OF PROFITS OR GAINS BROUGHT INTO CHARGE TO TAX, the person liable to make the annual payment is to be assessed and charged to tax as if no such payment was made, but is authorized to DEDUCT AND RETAIN TAX when making such payment. The recipient of the annual payment is bound to allow the deduction and to accept the net sum in satisfaction of the amount of the annual payment.

The right to deduct tax on interest paid out of "profits brought into charge to tax" refers to yearly interest only, although it does not matter whether the actual payment is made at more frequent intervals than a year. The question of what is "yearly interest" has been the subject of a number of decisions in the Courts, and the legal position is well summarised in *The Commissioners of Inland Revenue v. Sir Duncan Hay, Bart.* ((1924), 8 T.C. 636). In this case, unsecured loans which varied in amount had been in continuous existence for a number of years. There was no written agreement relating to the advances, and interest was charged annually at a rate which fluctuated with the Bank Rate. It was held that the interest on the advances was "yearly interest."

From a consideration of the opinions expressed in above case, the following propositions appear to be established :—

- (1) Interest payable in respect of short loans is not yearly interest (*Goslings and Sharpe v. Blake* (1889), 23 Q.B.D. 324).

(2) In order that the interest payable may be held to be yearly interest in the sense of the Income Tax Acts, the loan in respect of which interest is paid must have a measure of permanence.

(3) The loan must be in the nature of an investment (*Garston Overseers v. Carlisle* (1915), 3 K.B. 381).

(4) The loan must not be one repayable on demand (*Gateshead Corporation v. Lumsden* (1914), 2 K.B. 883).

(5) If in point of fact the interest is payable yearly, it may still be yearly interest even though the rate may fluctuate from time to time.

It will thus be seen that it is not essential that the rate of interest should be fixed, and that the chief element is the measure of permanence. Some difficulty may be encountered in practice in "borderline" cases, but it is at least certain that if the loan or the deposit is made for a fixed period of not less than one year, the interest is "yearly interest" and tax is properly deductible. This is borne out by the general custom of banks not to deduct tax from deposit interest where the deposit is repayable on demand or at short notice.

Interest on a loan for one year is annual interest. Interest on money employed or intended to be employed as capital in the business (as distinct from temporary accommodation) is not an admissible deduction from profits, whether it is an annual payment or not (*Ward v. Anglo-American Oil Co.* (1934), 19 T.C. 94).

Under General Rule 21, any person who pays any interest of money, annuity or other ANNUAL PAYMENT or patent royalty NOT PAYABLE or not wholly payable OUT OF PROFITS OR GAINS BROUGHT INTO CHARGE TO TAX MUST DEDUCT TAX *at the time of payment*, AND ACCOUNT FOR IT to the Inland Revenue.

Readers will note that General Rule 19 EMPOWERS deduction, whereas General Rule 21 DIRECTS deduction

of Income Tax at the source. Where a person applies his income in paying interest, General Rule 19 empowers him to deduct the tax and retain it and so recoup tax on the equivalent amount of his own income ; General Rule 21 directs him to deduct tax from interest not paid out of income and to pay the tax so deducted over to the Revenue.

Under General Rule 21, the payer must deduct the tax at the rate of tax in force at the time of the payment, and forthwith deliver to the Commissioners of Inland Revenue, for the use of the Special Commissioners, an account of the payment, or of so much thereof as is not made out of profits or gains brought into charge, and of the tax deducted. The Special Commissioners must then assess and charge the payment. Where no account or an unsatisfactory account is delivered, the Special Commissioners may make an assessment according to the best of their judgment. An assessment under Rule 21 is subject to the usual right of appeal.

The amount of annuities which an assurance company carrying on the business of granting annuities is entitled to treat as having been paid out of profits or gains brought into charge to tax, is not to exceed the amount of the taxed income of its annuity fund.

Capitalisation by mortgagees of arrears of mortgage interest is not to be regarded as payment by the mortgagor of such interest. The mortgagees in fact capitalise the interest because the mortgagor does *not* pay it, and in order to charge interest on the unpaid interest. A Rule 21 assessment cannot be made when the interest is capitalised in this way. When the interest is in fact paid out of capital (*e.g.*, by inclusion in a payment repaying the whole debt), a Rule 21 assessment can properly be made (*C.I.R. v.*



*Oswald (Cosier's Settlement Trustee)* (1945), T.R. 123), in which it was held that the important case of *C.I.R. v. Lawrence Graham & Co.* ((1937), 2 K.B. 179) was wrongly decided).

The Income Tax Codification Committee point out that General Rule 21 applies to "short" interest as well as to yearly interest, and tax should be deducted therefrom where the interest is not paid out of profits or gains brought into charge; in practice, however, the strict observance of the rule seems to be overlooked in many cases without serious effects, as most "short" interest arises in trading transactions, and appears in the accounts.

In certain circumstances, an expense may be deductible in arriving at the adjusted profits for the purposes of Case I or Case II of Schedule D, and yet be assessable under General Rule 21. The best example of this is where a company guarantees the dividend of another company. The net sums paid away under the guarantee, if wholly and exclusively laid out for the purposes of the trade, are allowable deductions in adjusting the paying company's profits, but are nevertheless "annual payments." Having been so allowed, the payments are not "paid out of profits brought into charge to tax," and the tax deducted in arriving at the net amounts is collected by an assessment under General Rule 21. The fact that the payments are variable and contingent does not affect their character as annual payments (*Moss Empires v. C.I.R.* (1937), A.C. 785).

Copyright royalties are not charged to tax by deduction except where the usual place of abode of the owner of the copyright is outside the United Kingdom, in which case General Rule 21 applies

(except in respect of copies of works exported for distribution outside the United Kingdom) (§ 25—1927). In such cases the agent paying the royalty is made liable for deducting the tax on the amount of the royalty as reduced by any agent's commission (§ 18—1930). Since the tax in such cases is always collected under General Rule 21, the copyright royalties are still deductible in the Profit and Loss Account of the publisher, even where he is the agent for the purposes of deduction and payment of the tax.

It is of the utmost importance that the reader should appreciate that by the expression "profits or gains brought into charge to tax" is meant the statutory income of the year, *before* deducting annual charges, irrespective of the amount of the actual profits (*Attorney-General v. Metropolitan Water Board* (1927), 13 T.C. 294; *Allchin v. South Shields Corporation* (*Coulthard*) (1943), T.R. 303).

For 1944-45 onwards, in determining whether Rule 21 applies, local authorities can set off interest they pay against their whole taxed income, irrespective of any restriction imposed by law on the application of monies belonging to the authority. (Before that year, an authority could only set off interest against income of the fund out of which the payment was made, unless it had a Private Act similar to the South Shields one.) Any beneficial occupation under Sch. A is to be regarded as profits available, but there must be excluded from income any sum which (a) has been or is to be reimbursed by the Crown or any other person, or (b) is taken into account in computing a deficiency which another person is under a legal obligation to make good to the authority, or (c) is charged to capital. Misc. Rule 6, Sch. D is repealed,

thus doing away with the charge on "the proper officer" for tax payable on interest charged on rates. (§ 21—(No. 2) 1945).

Where losses brought forward extinguish the assessment, there are no "profits or gains brought into charge to tax" within General Rule 19 (assuming no other statutory income), and any interest paid is chargeable under General Rule 21 (*Trinidad Petroleum Development Co. v. C.I.R.* (1937), 21 T.C. 1).

Where a statutory company is specifically authorised to pay interest out of capital and specifically does so, such interest is not to be deemed to be paid out of taxed profits, and a General Rule 21 assessment can be raised, although an adequate amount of taxed profits exists (*Central London Railway Co. v. Commissioners of Inland Revenue*, *London Electric Railway Co. v. same* (1936), 15 A.T.C. 231). Moreover, a repayment claim cannot succeed in respect of bank interest paid out of capital in such a case (*Metropolitan Railway Co. v. Commissioners of Inland Revenue* (1936), 15 A.T.C. 231). A similar position seems to arise in respect of interest paid on capital raised for the construction of works, etc., under Section 54, Companies Act, 1929, since this interest must be charged to capital.

It is sometimes contended that interest paid under Section 54, Companies Act, 1929, is in the nature of a dividend, to which General Rules 19 and 21 do not apply, but it is thought that this is not so, since the section expressly provides for *interest* being paid on the capital in point pending the earning of profits. The position does not appear to have been judicially interpreted.

One must not look for the fund of "profits or gains brought into charge to tax" within the meaning of General Rule 19 (1) outside the year in which the interest was paid and the tax deducted. The profits or gains brought into charge to tax mean the profits or gains as taxed by assessment or by deduction at source in the year of charge, and do not include any unexhausted balance of profits actually charged to tax in previous years (*Luipaard's Vlei Estate and Gold Mining Co. v. C.I.R.* (1930), 15 T.C. 573).

**Illustration.**

A.'s profits from his business, for the years ended 30th September, 1943, 1944 and 1945, were respectively £5,000, £150 and £4,000. His only other income was the Net Annual Value of his house, £100 and £50, dividends received under deduction of tax.

Each year he paid £640 loan interest.

Assessments :—	1944-45.	1945-46.	1946-47.
Case I, Schedule D ..	£5,000	£150	£4,000
Schedule A and taxed dividends .. .. .	150	150	150
	<hr/>	<hr/>	<hr/>
Profits or gains brought into charge to tax .. .. .	<u>£5,150</u>	<u>£300</u>	<u>£4,150</u>
A. therefore deducts tax under General Rule 19 on ..	£640	£300	£640
but under General Rule 21 on .. .. .		£340	

*i.e.*, although he made an *actual* profit in 1945 of £4,000, he had only £300 "brought into charge to tax" in that year, and must account under General Rule 21, for the tax on the balance of the annual charge. If the loan interest were paid wholly and exclusively for the purposes of the business, it could be set off against the 1946-47 assessment on the business under Case I, Schedule D, reducing it to £3,660 under § 19, 1928 (*see* Chap. VII, § 3).

Companies with international connections may issue debentures, etc., containing an option by which interest is payable in sterling or in foreign currency. The exact terms of the option must be regarded, but if, having regard to the terms, the primary obligation is to pay in sterling, the deduction of tax, and any General Rule 21 assessment are based on the interest calculated in sterling, only the net sum after deduction of tax being convertible into currency where the debenture holder exercises his option. If any debenture-holder by receiving currency obtains more than the sterling sum (*e.g.*, by reason of a different exchange rate when he cashes his interest-warrant), he can be assessed on the excess if the authorities are in a position to assess him (*Rhokana Corporation v. C.I.R.* (1938), A.C. 380).

Any person who refuses to allow any deduction of tax authorised by the Income Tax Acts is liable

to a penalty of £50. Every agreement for payment of interest, rent, or other annual payment in full without allowing any such deduction is void (General Rule 23) as regards that stipulation. An agreement to pay "interest (or rent) at such a rate (or of such an amount) as, after deducting tax at the rate or rates for the time being in force, shall leave a clear annual rate (or amount) of . . . ." does not contravene Rule 23, and is valid.

An agreement which states that an annual payment is to be "free of tax" contravenes General Rule 23 and the payer is entitled to deduct tax in the usual way; but if it can be shown that the agreement so worded does not carry out the intention of the parties, the Court may allow the agreement to be rectified by inserting wording similar to that indicated in the preceding sentence (*Jervis v. Howle and Talke Colliery Co.* (1937), Ch. 67). There must be proof beyond fair and reasonable doubt that the true intention of the parties was not properly set out in the deed, otherwise a claim for rectification will fail (*Fredensen v. Rothschild* (1941), 20 A.T.C. 1).

(As to the reduction of the amount payable for 1941-42 onwards in the case of agreements to pay fixed net sums, see Chap. XI, § 11.)

#### (b) Effect on Allowances.

The business assessment for the current Income Tax year is based normally upon the adjusted profits of the previous accounting year, and in arriving at these profits there will have been added back the interest paid in that accounting year. In arriving at the statutory total income for the purposes of allowances, however, there must be deducted from the assessment

plus other income the annual charges FOR THE YEAR OF ASSESSMENT (not those added back in the accounts forming the basis of assessment). The Earned Income Allowance in particular may be restricted as shown in the following illustration.

Concisely stated, the position is that in so far as interest or other annual charges are paid in the year, the taxpayer has been making income for the payee. To the extent that he has been able to make the payment out of unearned income, the Earned Income Allowance will not be affected, but to the extent that the payment exceeds the unearned income, it must have come out of earned income. The taxpayer can only get allowances off his own income, hence where the statutory total income is less than the earned income, the earned income allowance is granted only on the lower figure. The total allowances cannot exceed the statutory total income.

#### Illustration.

Dr.		PROFIT AND LOSS ACCOUNT		Cr.	
For the Year ended 31st March, 1947.					
To Rent .. .. .	£	120	By Gross Profit .. .. .	£	1,496
„ Office Expenses .. .. .	360				
„ Salaries .. .. .	210				
„ Interest on Loan .. .. .	500				
„ Profit .. .. .	306				
	<u>£1,496</u>				<u>£1,496</u>

#### INCOME TAX COMPUTATION, 1947-48.

Net Profit for year to 31st March, 1947 ..	£306
Add Interest on Loan charged in accounts	<u>£500</u>

Adjusted profit .. ..	<u>£806</u>
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Assessment 1947-48 ..	<u>£806</u>
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(a) Assume that X, the owner of the business, is a married man with three children under 16, and has no other source of income, and that the interest payable for the year to 5th April, 1948, is

£400. Since he pays away £400 as annual interest, his statutory total income is only £406, and it is only on his own income that he can get allowances. His assessment will therefore be as follows :—

1947-48.	£
Sch. D, Case I—preceding year's profits	806
<i>Deduct</i> Allowances—	£
Earned Income $\frac{1}{8}$ th of £406 ..	68
Personal .. .. .	180
3 Children, £180 but limited to	158
	<hr/> 406
To be kept in charge	<u>£400</u>
Chargeable—	
£400 at 9/- .. ..	<u>£180 0 0</u>

He cannot obtain the full children's allowance, nor any reduced rate relief, as the £400 of his income which he earns for someone else must be "kept in charge" under General Rule 19, at the standard rate.

(b) Assuming X had dividend income (taxed at source) amounting to £250 gross, and the interest payable to remain at £400, he would be assessed as follows :—

1947-48.	£
Sch. D, Case I .. .. .	806
<i>Deduct</i> Allowances—	
Earned Income $\frac{1}{8}$ th of £656 ..	£110
Personal .. . . .	180
3 Children .. . . .	180
	<hr/> 470
	<u>£336</u>
Chargeable—	
£50 at 3/- .. . . .	£7 10 0
£75 at 6/- .. . . .	22 10 0
£211 at 9/- .. . . .	94 19 0
	<hr/> £124 19 0

In this case, £250 of the annual interest is covered by unearned income, leaving £150 paid out of earned income.

(c) If X's other income exceeds £400, he is entitled to the earned income allowance on the whole £806.

## Proof of (a) and (b).

	(a)	Tax.	(b)	Tax.
	£	£ s. d.	£	£ s. d.
Sch. D, Case I .. ..	806		806	
Dividends .. ..	—		250	112 10 0
			<u>1,056</u>	
Less Annual Interest ..	400	180 0 0	400	180 0 0
	<u>406</u>	<u>*180 0 0</u>	<u>656</u>	<u>*07 10 0</u>
Deduct Allowances :—				
Earned Income .. ..	£68		£110	
Personal .. ..	180		180	
Children .. ..	158		180	
	<u>406</u>		<u>470</u>	
	<u>Nil</u>		<u>£186</u>	
At 3/- .. ..			£50	£7 10 0
At 6/- .. ..			75	22 10 0
At 9/- .. ..			61	27 9 0
				<u>57 9 0</u>
Tax payable under Sch. D.		<u>£180 0 0</u>		<u>£124 19 0</u>

\*Tax to be accounted for.

## (c) Interest received Gross.

Interest on deposits, discounts on Treasury Bills, interest from Co-operative Societies, interest received gross on Registered or Inscribed  $3\frac{1}{2}\%$  War Stock,  $3\%$  Defence Bonds or other issues issued with like privileges, and small dividends on other Government Securities received gross, are assessable under Case III of Schedule D on the basis outlined in Chap. V, § 1.

In the ordinary way, trade interest, interest on deposit, etc., is brought in for Income Tax purposes in the accounts of the business, but where any interest is separately assessed as above indicated, it must be excluded from the profits brought into assessment.

## § 7.—Change in date to which Accounts are made up, etc.

When a taxpayer changes the date to which he makes up his accounts, with the result that an account for less or more than one year is made up in order to bring the new accounting date into operation, the Commissioners of Inland Revenue are given power to decide what shall be the twelve months' period ending



in the previous year which shall be considered as the basic period for arriving at the assessment (§ 34—1926 ; § 14—1930). The rules are as follows :—

Where an account has or accounts have been made up to a date or dates within the period of three years immediately preceding the year of assessment—

- (a)—(i) if an ACCOUNT WAS MADE UP TO A DATE WITHIN THE YEAR PRECEDING THE YEAR OF ASSESSMENT, and  
(ii) that account was the ONLY ACCOUNT made up to a date in that year, and  
(iii) was for a PERIOD OF ONE YEAR, BEGINNING either at the COMMENCEMENT OF THE TRADE, profession, vocation or occupation, OR AT THE END OF THE PERIOD ON THE PROFITS or gains OF WHICH THE ASSESSMENT FOR THE LAST PRECEDING YEAR of assessment WAS TO BE COMPUTED, the profits or gains shown by that account are to be taken to be the profits or gains of the year preceding the year of assessment ;
- (b) in any other case the Commissioners of Inland Revenue are to decide what period of twelve months ending on a date within the year preceding the year of assessment shall be deemed to be the year the profits or gains of which are to be taken as the basis of the assessment.

Where the Commissioners of Inland Revenue have given a decision under (b) above and it appears to them that in consequence the tax for the last PRECEDING YEAR OF ASSESSMENT in respect of the profits or gains from the same source should be COMPUTED on the profits or gains of a CORRESPONDING PERIOD, they may give directions to that effect and an assessment or additional assessment or repayment of tax must be made accordingly. An appeal can be made in the usual way against any such additional assessment.

The decision of the Commissioners as to the date to be taken under these rules will involve “splitting” profits of the periods for which accounts have actually been made up. It is provided that the profits are to be apportioned on a “time” basis, in proportion to the number of months or fractions of months in the respective periods (§ 35—1926). In practice, fractions of months are usually ignored unless their inclusion would make an appreciable difference to the amounts involved.

Summarising the rules, it is found that in order that an account shall be taken as the basic period on which to found an assessment —

- (1) The account must end in the previous year of assessment ;
- (2) It must be the only account ending in that year ;
- (3) It must be an account for a period of twelve months ; and
- (4)—(a) If it is the first account of the business, it must have commenced when the business commenced.  
(b) If it is not the first account, it must have commenced on the date to which the basic twelve months were taken for the purposes of the previous year's assessment.

If any one or more of these conditions is not satisfied, the Commissioners of Inland Revenue are to choose a date in the previous year and build up twelve months' profits (by splitting accounts) to that date. They may then adjust the previous year's assessment on a corresponding basis.

It will be seen that the powers given to the Commissioners of Inland Revenue do not apply if no account at all has been made up within the previous three years. In that case the assessing Commissioners (General or Special, as the case may be) will make estimated assessments.

The following is an official note setting out briefly the practice of the Board of Inland Revenue in cases where a trader permanently changes his accounting date :—

“ The relevant statutory provisions are contained in Section 34 of the Finance Act, 1926 (as amended by Section 14 of the Finance Act, 1930). The effect of these provisions is briefly as follows :—

- (i) In the normal case where there is only one account ending in the year preceding the year of assessment and that

- account is for a period of one year, the assessment is to be based on the profit of that account. (Section 34 (1) (a).)
- (ii) In other cases, the Board of Inland Revenue are to decide what period of 12 months ending on a date in the preceding Income Tax year is to be basis year. (Section 34 (1) (b).)
  - (iii) Where the Board have determined the basis year for any Income Tax year under (ii), they may direct that the assessment for the preceding Income Tax year is to be adjusted to the profits of the corresponding period, *i.e.*, the year ending on the same date in the previous year (Section 34 (2)); an appeal against any such direction lies to the General or Special Commissioners, who are empowered to grant 'such relief, if any, as is just.' (Section 34 (3).)

"Under Section 34 (1) (b) the Board normally decide that the assessment is to be based on the profits of the period of 12 months ending on the new accounts date in the preceding Income Tax year, *i.e.*, the date to which the trader proposes to make up his accounts in future.

"The question then arises whether there is to be any adjustment of the assessment for the preceding Income Tax year under Section 34 (2) to the profits of the 'corresponding' period. Such an adjustment may increase or decrease the liability, according to the trend of profits.

"The considerations which the Board have in mind in determining this question are as follows :—

"Where there is a permanent change of accounting date then, whether or not revision under Section 34 (2) is ordered, one of two things must, in the ordinary course, happen :—

- (a) If the new date is later in the Income Tax year than the old, the profits of some period will not come into assessment at all.
- (b) If the new date is earlier in the Income Tax year than the old, the profits of some period will come into assessment twice.

"If the profits of the period omitted were relatively low, or the profits of the period coming in twice were relatively high, the Revenue would gain : conversely, if the profits of the period omitted were relatively high, or the profits of the period coming in twice were relatively low, the taxpayer would gain. The Board attempt to secure that the profits to be assessed twice, or to be omitted from assessment, as the case may be, are 'average' profits. As a rule this object can be secured neither by straightforward revision nor by non-revision, but only by taking for the year to which Section 34 (2) applies some figure intermediate between the revised and unrevised figures, and it is the Board's normal practice to propose, subject to the concurrence of the Commissioners of Income Tax

having jurisdiction in the particular case under Section 34 (3), the adoption of such an intermediate figure. That intermediate figure is computed by reference to a consideration of—

- (i) the profits of all the accounting periods of which any part enters into either the basis year (or, in some cases, years) under Section 34 (1) (b) or the 'corresponding period' under Section 34 (2); and
- (ii) the number of years for which the assessments are based in whole or in part on any of the profits of such accounting periods.

"The aggregate profit of the accounting periods falling within sub-para. (i) is expanded or reduced on a time basis so as to give a proportionate figure for the number of years of assessment falling within sub-para. (ii), and the assessment for the year to which Section 34 (2) applies is adjusted, up or down as the case may be, so that the total of the assessments for all the years falling within sub-para. (ii) is precisely equal to the proportionate figure computed as explained above. The working of this practice can best be illustrated by examples and four such examples will be found below.

"It is open to the taxpayer, if he does not accept the Board's proposal, to appeal to the General or Special Commissioners against any direction by the Board that may be made under Section 34 (2) or against an omission to issue a direction, and the Commissioners, by Section 34 (3), are empowered on appeal to give such relief as is just. The Board's proposal represents the solution which they consider would be likely to commend itself to the Commissioners and where it is accepted there is in effect an agreed recommendation as to what is thought to be just.

"The practice outlined above is suitable for the majority of cases. There are, however, certain classes of case which are incapable of solution along these lines for which modifications are necessary, *e.g.* :—

- (a) cases where the 'average' computation brings out a figure for the adjusted preceding year assessment which is not intermediate between the unrevised figure and the profit of the 'corresponding period';
- (b) cases where there is a marked seasonal fluctuation in the rate of profit (*e.g.*, as in the case of the seaside hotel);
- (c) cases where in some or all of the periods concerned losses were incurred;
- (d) cases where any one of the years concerned is affected by the commencement or cessation provisions.

"The modifications that are introduced to deal with these special types of case cannot be described in detail within the limits of this brief Note, but the general principle followed throughout is

that of equating the average rate of assessments over the years affected to the average rate of profits in the accounting periods that form the basis of those assessments. In cases falling within head (a) it may be necessary in order to secure this result to depart from the general rule mentioned above and to determine a basis year under Section 34 (1) (b) which, when regard is had to the profits of that year and its 'corresponding period,' will enable effect to be given to the 'average' adjustment. Again in cases falling within head (b) it may be necessary to modify the 'average' adjustment so that the assessments reflect a true annual rate of profit and not a rate that is inflated or depressed by seasonal results.

"Where the 'average' computation brings out a figure for the adjusted preceding year assessment which exceeds, or falls short of, the unrevised figure for that year by a relatively small amount, it is not the Board's normal practice to take any action by way of 'average' adjustment. For this purpose the Board would normally regard as relatively small a difference that did not exceed ten per cent. of the average of the current and preceding years' assessments and was less than £1,000.

"The examples given are as follows :—

"Example A.

				<i>Profits</i>
12 months to	30th Sept., 1941	..	..	£36,000
12	..	..	30th Sept., 1942	18,000
9	..	..	30th June, 1943	12,000

30th June is to be the future accounting date.

"1944-45. The Board decide that the assessment should be on the profits of the year to 30th June, 1943, *i.e.*,  
 $£12,000 + \frac{1}{4} \text{ of } £18,000 = £16,500$

"1943-44. The assessment will originally have been made on the profits of the year to 30th Sept., 1942, *i.e.*, on £18,000.

"The profits of the 'corresponding period,' *i.e.*, the year to 30th June, 1942, are :—

$\frac{3}{4}$ of £18,000	..	..	..	=	£13,500
$\frac{1}{4}$ of £36,000	..	..	..	=	9,000
Total					<u>£22,500</u>

"Revision of the basis under Section 34 (2) would therefore involve an additional assessment of £4,500 (£22,500—£18,000).

"In this case the accounting periods of which all or part enters into the 'basis period' or the 'corresponding period' comprise the 33 months to 30th June, 1943, while the assessments which may be affected by the profits of those accounting periods are those for the three years 1942-43 to 1944-45. Consequently the Board would

propose an adjustment in the 1943-44 assessment of such an amount that the assessments for 1942-43, 1943-44 (as revised) and 1944-45 would be exactly equal to three years' profits at the average rate of the actual profits for the 33 months to 30th June, 1943. This would lead to a limitation of the additional assessment for 1943-44 to £1,500 computed as follows :—

Total profits for 33 months to 30th June 1943	.. .. .	£66,000
Profits for 36 months at the same rate		
( $\frac{33}{36} \times £66,000$ )	.. .. .	£72,000
Assessed 1942-43	.. .. .	£36,000
Assessed 1944-45	.. .. .	16,500
		<u>52,500</u>
Balance to be assessed for 1943-44	.. .. .	19,500
Deduct first assessment	.. .. .	18,000
		<u>Additional assessment .. £1,500</u>

“ Example B.

		<i>Profits</i>
12 months to 30th Sept., 1941	.. .. .	£12,000
12 „ „ 30th Sept., 1942	.. .. .	30,000
9 „ „ 30th June, 1943	.. .. .	24,000

30th June is to be the future accounting date.

“ 1944-45. The Board decide that the assessment should be on the profits of the year to 30th June, 1943, *i.e.*,

$$£24,000 + \frac{1}{4} \text{ of } £30,000 = £31,500$$

“ 1943-44. The assessment will originally have been made on the profits of the year to 30th Sept., 1942, *i.e.*, on £30,000.

“ The profits of the ‘corresponding period,’ *i.e.*, the year to 30th June, 1942, are :—

$\frac{3}{4}$ of £30,000	=	£22,500
$\frac{1}{4}$ of £12,000	=	3,000
		<u>Total £25,500</u>

“ Revision of the basis under Section 34 (2) would therefore involve a reduction of £4,500 (£30,000—£25,500).

“ In this case the accounting periods of which all or part enters into the ‘basis period’ or the ‘corresponding period’ comprise the 33 months to 30th June, 1943, while the assessments which may be affected by the profits of those accounting periods are those for

the three years 1942-43 to 1944-45. Consequently the Board would propose an adjustment in the 1943-44 assessment of such an amount that the assessments for 1942-43, 1943-44 (as revised) and 1944-45 would be exactly equal to three years' profits at the average rate of the actual profits for the 33 months to 30th June, 1943. This would lead to a reduction of £1,500 for 1943-44 computed as follows :—

Total profits for 33 months to 30th June,			
1943	..	..	£66,000
Profits for 36 months at the same rate :			
( $\frac{36}{33} \times £66,000$ )	..	..	£72,000
Assessed 1942-43	..	£12,000	
Assessed 1944-45	..	31,500	
			<u>43,500</u>
Balance to be assessed for 1943-44	..		28,500
First assessment for 1943-44	..		<u>30,000</u>
		Reduction	<u>£1,500</u>

#### “Example C.

			<i>Profits</i>
12 months to	30th Sept., 1941	..	£14,000
12	„	30th Sept., 1942	30,000
6	„	31st March, 1943	22,000

31st March is to be the future accounting date.

“1943-44. The Board decide that the assessment should be on the profits of the year to 31st March, 1943, *i.e.*,

$$£22,000 + \frac{1}{2} \text{ of } £30,000 = £37,000$$

“1942-43. The assessment will originally have been on the profits of the year to 30th Sept., 1941, *i.e.*, on £14,000.

“The profits of the ‘corresponding period,’ *i.e.*, the year to 31st March, 1942, are :—

$$\begin{aligned} \frac{1}{2} \text{ of } £30,000 &= £15,000 \\ \frac{1}{2} \text{ of } £14,000 &= 7,000 \end{aligned}$$

$$\text{Total} \quad \underline{\underline{£22,000}}$$

“Revision of the basis under Section 34 (2) would therefore involve an additional assessment of £8,000 (£22,000—£14,000).

“In this case the accounting periods of which all or part enters into the ‘basis period’ or the ‘corresponding period’ comprise the 30 months to 31st March, 1943, while the assessments which may be

affected by the profits of those accounting periods are those for the two years 1942-43 and 1943-44. Consequently the Board would propose an adjustment in the 1942-43 assessment of such an amount that the assessments for 1943-44 and 1942-43 (as revised) would be exactly equal to two years' profits at the average rate of the actual profits for the 30 months to 31st March, 1943. This would lead to a limitation of the additional assessment for 1942-43 to £1,800 computed as follows :—

Total profits for 30 months to 31st March,	
1943 .. .. .	<u>£66,000</u>
Profits for 24 months at the same rate :	
(24/30ths of £66,000) .. ..	£52,800
Assessed 1943-44 .. .. .	<u>37,000</u>
Balance to be assessed for 1942-43 ..	15,800
Deduct first assessment .. ..	<u>14,000</u>
Additional assessment ..	<u>£1,800</u>

“ Example D. .

		<i>Profits</i>
12 months to 31st March, 1941 .. ..		£1,600
12 „ „ 31st March, 1942 .. ..		3,200
15 „ „ 30th June, 1943 .. ..		2,400
30th June is to be the future accounting date.		

“ 1944-45 and 1943-44. In this case a decision under Section 34 (1) (b) has to be given for two years. The Board decide that the assessment for the year 1944-45 should be on the profits of the year to 30th June, 1943, and that the assessment for the year 1943-44 should be on the profits of the year to 30th June, 1942.

1944-45	12/15ths of £2,400	=	£1,920
1943-44	3/15ths of £2,400 + 9/12ths of £3,200 = £480 + £2,400	=	2,880

“ 1942-43. The assessment will originally have been on the profits of the year to 31st March, 1942, *i.e.*, on £3,200.

“ The profits of the ‘corresponding period,’ *i.e.*, the year to 30th June, 1941, are :—

3/12ths of £3,200	=	£800
9/12ths of £1,600	=	<u>1,200</u>
		<u>£2,000</u>

“ Revision of the basis under Section 34 (2) would therefore involve a reduction of £1,200.



“ In this case the accounting periods of which all or part enters into the ‘ basis periods ’ or the ‘ corresponding periods ’ comprise the 39 months to 30th June, 1943, while the assessments which may be affected by the profits of those accounting periods are those for the four years 1941-42 to 1944-45. Consequently the Board would propose an adjustment in the 1942-43 assessment of such an amount that the assessments for 1941-42, 1942-43 (as revised), 1943-44 and 1944-45 would be exactly equal to four years’ profits at the average rate of the actual profits for the 39 months to 30th June, 1943. This would lead to a reduction in the assessment for 1942-43 of £738, computed as follows :—

Total profits for 39 months to 30th June,			
1943	. . . . .		<u>£7,200</u>
Profits for 48 months at the same rate :			
(48/39ths × £7,200)	. . . . .		£8,862
Assessed 1944-45	. . . . .	£1,920	
1943-44	. . . . .	2,880	
1941-42	. . . . .	1,600	
		<hr/>	6,400
Balance to be assessed for 1942-43	. . . . .	£2,462	
First assessment	. . . . .	3,200	
		<hr/>	
	Reduction	. . . . .	<u>£738</u> ”

### § 8.—New Businesses.

In respect of the early years of a business, special rules are provided for arriving at the assessments, and for allowing a measure of relief in cases where the profits of the second and third years of assessment fall short of the assessments on the statutory bases, as follows :—

- (1) First year—actual profits from the date of commencement to 5th April following.
- (2) Second year—profits of twelve months from the date of commencement.

- (3) Thereafter—profits of previous year (Cases I and II, R. 1 (2); §§ 29 and 36—1926).
- (4) The taxpayer can claim that the assessments for the second and third years shall be adjusted to the actual profits of those fiscal years. (He must claim for both years or not at all.) The claim must be made to the Inspector of Taxes in writing within two years after the end of the second year of assessment and can be revoked within one year after the end of the third year of assessment (§ 15—1930).

If the first account is for less than a year, then a due portion of the second account must be taken in order to build up the profits of 12 months from the date of commencement (*Manson v. Perry's (Ealing) Ltd.* (1931), 16 T.C. 60).

It will be seen that the accounts for the first year of the business will give normally the assessments for the first three years of assessment.

#### Illustration.

A commenced business on 1st June, 1945. The accounts for the year to 31st May, 1946, showed an adjusted profit of £400.

#### ASSESSMENTS.

1945-46	Actual profits from 1st June, 1945, to 5th April, 1946, 10 months— $\frac{10}{12}$ ths of £400	.. ..	£333
1946-47	Profits for one year from 1st June, 1945	.. ..	£400
1947-48	Profits of accounting year ended in the preceding year, i.e., year to 31st May, 1946	.. ..	£400

The assessments for the second and third years of assessment are thus, normally, in the same amounts, being based on the first year's accounts. Where the profits of the first year are not maintained, this result would be a hardship, and it is for that reason that the relief mentioned in (4) above is provided.

Where it is necessary to take a period which differs from an accounting period, the figures shown by the accounts which cover the period are apportioned on a "time" basis, in months and fractions of months.

The first account is not always made up for the period of one year, as the date selected as the accounting date for future years will usually determine the date to which the first account is made up, *e.g.*, if 31st December is chosen as the accounting date, the first account will be for more or less than a year unless the business commenced on 1st January. In such a case, the assessment for the third year will be based on the profits of twelve months ended on a date in the preceding year chosen by the Commissioners of Inland Revenue (*see* § 7 of this Chapter). The practice is normally as follows:—

- (a) If annual accounts are to be made up to the same date in future, the assessment is based on the profits of the year ended on that date in the second year of assessment (even if accounts were made up to some other date in that year).
- (b) If, however, the period from the commencement of the business to the date in the second year which is chosen as the accounting date for the future is less than twelve months, the assessment for the third year is based on the profits of the first twelve months.
- (c) If future accounts will be made up to varying dates, a mutually convenient date is usually agreed with the Inspector.

#### Illustrations.

(1) N commenced business on 1st January, 1944, his profits for the years ended 31st December, being:—1944, £2,400; 1945, £3,000; 1946, £100. His assessments would be as follows:—

Year of Assessment.	Original Assessment.	Assessment as amended under § 15—1930.
1943-44	$\frac{1}{2}$ of £2,400 = £600	(not applicable.)
1944-45	£2,400	$\frac{1}{2}$ of £2,400 + $\frac{1}{2}$ of £3,000 = £2,550
1945-46	£2,400	$\frac{1}{2}$ of £3,000 + $\frac{1}{2}$ of £100 = £2,275
1946-47	£3,000	(not applicable.)
1947-48	£100	do.

In this case, the result of the adjustment under § 15, 1930 would be to increase the assessments for the two years 1944-45 and 1945-46 by £25 net, and as this would increase the tax payable, a claim would not be made.

Care must be taken to watch the effect of changes in the rate of tax, *e.g.*, if the years were 1945-46 and 1946-47 and there was a decrease of £2,000, and an increase of £2,040 respectively, the effect of a claim under § 15, 1930 would be :—

1945-46	Decrease of £2,000 at 10/- .. ..	=	£1,000	0	0
1946-47	Increase of £2,040 at 9/- .. ..	=	918	0	0
Net decrease in tax payable .. ..			<u>£82</u>	<u>0</u>	<u>0</u>

In spite, therefore, of the net increased assessments, it would pay to claim.

(2) T Ltd. commenced business on 1st June, 1944. His profits were as follows :—

Seven months ended 31st December, 1944 ..	£700
Year ended 31st December, 1945 .. ..	£2,400
“ “ “ 1946 .. ..	£1,800
“ “ “ 1947 .. ..	£960

#### ASSESSMENTS.

1944-45	On the actual profits, <i>i.e.</i> , £700 + $\frac{2}{12}$ ths of £2,400	=	£1,300
1945-46	On the profits of twelve months from the period of commencement, <i>i.e.</i> , £700 + $\frac{5}{12}$ ths of £2,400	=	£1,700
1946-47	Since the accounts for the year ended 31st December, 1945, began neither at the date when the business commenced nor at the date to which was taken, the period on which the 1945-46 assessment was based, the Commissioners of Inland Revenue must choose the basic twelve months ( <i>see</i> Chap. IV, § 7). They would normally take the accounts to 31st December, 1945, as 31st December is to be the future accounting date .. ..	=	£2,400

At any time before 6th April, 1948, the taxpayer may elect to be assessed upon the actual profits of 1945-46 and 1946-47, as follows :—

1945-46  $\frac{9}{12}$ ths of £2,400 +  $\frac{3}{12}$ ths of £1,800 = £2,250.

1946-47  $\frac{9}{12}$ ths of £1,800 +  $\frac{3}{12}$ ths of £960 = £1,590

resulting in a saving of the tax on £(1,700 + 2,400) — £(2,250 + 1,590) = £260. As explained in the previous illustration, not only the amount of the assessments, but the rates of tax should be taken into consideration, before deciding whether or not to claim an adjustment to "actual."

When claiming relief, the effect on the "basis period" for allowances under the Income Tax Act, 1945, must be considered.

## § 9.—Discontinuance of Business.

### (a) Adjustment of Assessments.

Upon the discontinuance of a business, the assessment is adjusted to the actual profits of that year of assessment, *i.e.*, from the 6th April to the date of discontinuance, whether this is more or less than an assessment based on the previous year's profits. Further, the Commissioners may increase the assessment for the year before the year of discontinuance (*i.e.*, the penultimate year) to the actual profits of that year of assessment, where such profits are greater than the assessment based on the profits of the previous year, but there is no corresponding right to the taxpayer to have the assessment reduced where the actual profits are lower than the assessment (§ 31—1926). By the profits of the penultimate year is meant the apportioned profits from 6th April to 5th April (*Manson v. Wesley* (1931), 16 T.C. 654).

### Illustrations.

(1) X discontinued business on the 30th September, 1946.

His adjusted profits were as follows :—

Year ended 31st December,	1943	..	£800
" " " "	1944	..	£1,000
" " " "	1945	..	£600
Period ended 30th September,	1946	..	£400

## ASSESSMENTS.

1944-45	Preceding year's profits .. .. .	£800
1945-46	do. .. .. .	£1,000
1946-47	Actual profits $\frac{3}{4}$ ths of £400 .. .. .	£267

Since the profits for the penultimate year 1945-46, viz.,  $\frac{3}{4}$ ths of £800 +  $\frac{3}{4}$ ths of £400 = £583, are less than the assessment, £1,000, there is no adjustment of the 1945-46 assessment (unless the diminution of earned income relief owing to war conditions can be claimed; see Appendix XIII).

(2) K Ltd., discontinued business on 1st February, 1946.

Its profits were as follows:—

Year ended 30th September, 1942 ..	£1,700
do. 1943 ..	£1,200
do. 1944 ..	£1,800
do. 1945 ..	£900
Period ended 1st February, 1946 ..	£100

## ASSESSMENTS.

1943-44	Preceding year's profits .. .. .	£1,700
1944-45	do. .. .. .	£1,200
1945-46	Actual profits $\frac{5}{12}$ ths of £900 + £100 =	£550

An additional assessment of £150 is then raised to bring the assessment for 1944-45 up to the actual profit of the penultimate year, i.e., the year ended 5th April, 1945, viz.,  $\frac{5}{12}$ ths of £1,800 +  $\frac{5}{12}$ ths of £900 = £1,350.

Great care must be taken in deciding upon the date for discontinuance, e.g., by discontinuance on 31st March in lieu of 30th April, or *vice versa*, a considerable amount of Income Tax may be saved. In general terms, if the profits are falling it is better to discontinue at once; if they are rising, it will often pay to postpone discontinuance until after 5th April. Everything depends upon the exact facts, and in every case the alternative assessments should be computed before a decision is made.

Difficult questions sometimes arise as to the date of discontinuance; if stock is realised after the stated date of retirement of the owner of the business, it is entirely a question of fact for the decision of the Commissioners (General or Special) as to whether trading is continued during the period of realisation (*O'Kane & Co. v. C.I.R.* (1919-22), 12 T.C. 303).

If, after the dissolution of a partnership, the offices are kept open for the receipt and payment of accounts and carrying out existing contracts, the firm is assessable after dissolution if it is in fact *trading*, i.e., the rounding off of transactions, even in the total absence of buying and selling, may be trading (*Hillerns & Fowler v. Murray* (1932), 17 T.C. 77).

In the case of a company incorporated to manufacture, buy, sell, hire and let on hire, wagons, etc., wagons were manufactured and sold either outright or on hire purchase, or let out on hire. The wagons built to be let out on hire were capitalised in the books at a figure including manufacturing profit. These wagons were depreciated each year. The company decided to discontinue the hire business and sold off the wagons used in this branch of their business at a sum in excess of the book value, and it was held that as the object of the company was to make a profit out of the wagons, the profit was assessable (*Gloucester Railway Carriage and Wagon Co. v. C.I.R.* (1923-25), 12 T.C. 720).

Where a trader or follower of a profession or vocation goes out of business and there remain to be collected sums owing for goods supplied, or for services rendered, there is no question of assessing those receipts; they are covered by the assessments made during the life of the business whether the assessment was made on the basis of bookings or of receipts (*Bennett v. Ogston* (1930), 15 T.C. at p. 378). Although accounts have been kept and assessments made on a cash basis, therefore, no assessments can be made in respect of cash collected from debtors after the date of discontinuance of the business, unless an agreement to that effect was made as a condition of the adoption of the cash basis.

The assessment for the penultimate year is not to be increased where the discontinuance is in consequence of nationalisation schemes (§ 32—1946).

#### (b) Valuation of Trading Stocks.

Where a trade is discontinued *otherwise than by the death of a sole trader*, any trading stock must be

valued for the purposes of the accounts to the date of discontinuance, according to the following rules:—

*Circumstances.*

*Basis of Valuation.*

- |  |  |
|--|--|
| <p>(a) If sold or transferred for valuable consideration to a person who carries on or intends to carry on a trade in the United Kingdom, in such circumstances that the cost will be charged in the purchaser's accounts as an allowable expense.</p> <p>(b) In the case of any other trading stock (this will include a sale to another trader who acquires the stock as a fixed asset).</p> | <p>The sale price or value of the consideration.</p> <p>The amount it would have realised if sold in the open market at the discontinuance of the trade.</p> |
|--|--|

Any questions under (a) are to be determined by the General Commissioners where both trades are in the same jurisdiction, unless all parties agree to refer to the Special Commissioners. In any other cases, any questions are to be determined by the Special Commissioners. The term "trading stock" includes goods held for sale, raw materials and partly manufactured goods (§ 26—1938). On the death of a sole trader, the above provision does not apply, and the closing stock is valued on the usual basis.

## § 10.—Change in Ownership of a Business.

### (a) *Successions and changes in partnerships.*

The following are the rules for determining the assessments where there is a change in the proprietorship of a business (Sch. D, Cases I and II, R. 11; § 32—1926; § 16—1930):—

- (1) If a change occurs in a partnership of persons engaged in any trade, profession or vocation, by reason of
- (a) retirement or death of a partner, or
  - (b) the partial dissolution of the partnership, or
  - (c) the admission of a new partner,
- in such circumstances that



- (i) one or more of the persons who until that time were engaged in the trade, etc., continue to be engaged therein, or
- (ii) a person who until that time was engaged in any trade, etc., on his own account continues to be engaged in it, but as a partner in a partnership,

the assessments continue to be made on the business profits as if the business had continued without any change. If they so desire, however, THE PERSONS WHO WERE ENGAGED IN THE TRADE, profession or vocation *both immediately before and immediately after the change* may require THAT THE BUSINESS PROFITS SHALL BE ASSESSED AS IF THE TRADE, etc., HAD BEEN DISCONTINUED at the date of the change, AND A NEW TRADE, etc., had been then set up or COMMENCED. The notice must be signed by all of them and sent to the Inspector of Taxes within twelve months after the date of the change. Where any person involved is dead, his personal representative is the person to sign the notice on his behalf.

Where there is a change in a partnership, any notice requiring the assessments for the second and third years of ownership of the business to be adjusted to the actual profits must be signed by all the persons who were partners at any time between the commencement of the second year of assessment and the giving of the notice, or if a notice is given after the end of the third year of assessment, by those who were partners at any time during the second or third year of assessment (§ 15—1930).

(2) If in any other circumstances any person or partnership succeeds to any trade, profession or vocation which until that time was carried on by another person or partnership, the tax payable for all years of assessment must be computed as if the business had been discontinued and a new business commenced on the date of the succession.

Wherever, therefore, there is a succession to a business, the assessments are made as for a business discontinued and a new business started on the date of the succession, except in the case where there is at least one person continuing as owner or part owner (*i.e.*, where there is a change in a partnership, or a partner is admitted by a sole trader), in which case the assessments continue on the preceding year basis unless all persons engaged in the business, both before and after the succession, give notice that they want to be assessed as if there had been a discontinuance and recommencement.

The "partnership" provision does not cover the case of a partnership being dissolved and one of the partners continuing to carry on the business by himself as an individual, although in practice it is normally treated as if it did.

In those cases where the preceding year basis continues, the Inspector must (within four months from 5th April following the change) certify to the General Commissioners the particulars of the change, and the Commissioners must then notify the respective persons of a meeting of the Commissioners to consider the Inspector's certificate. After examination of the persons (if they attend) or on other satisfactory proof of the facts, the Commissioners must split the assessment between the old and the new partnerships on a fair basis. The determination of the Commissioners is final (Sch. D, Cases I and II, R. 9). Any doubt as to whether R. 9 still applies was resolved by the House of Lords (*R. v. City of London Income Tax Commissioners ; Ex parte Gibbs* (1942), T.R. 35).

Normally, the assessment is apportioned between the old and new firms on a time basis, but a turnover or other fair basis may be adopted if the Commissioners think fit. The "split" is usually agreed with the Inspector of Taxes, and attendance before the Commissioners is then unnecessary.

One very important case has arisen on the amended Rule 11. Changes in a partnership took place in successive years. On the first change, no notice was given to have the business assessed on the "discontinued and new" basis, but such notice was given on the second change. It was held that this notice affected only the second and third firms, but that since the first firm had given no notice, no amendment of assessments thereon could be made (*Osler v. Hall & Co.* (1932), 17 T.C. 68).

**Illustration.**

The firm of X and Y made the following profits :—

Year ended 31st December, 1943	£6,000
do. 1944	£10,000
do. 1945	£50,000

On 1st January, 1946, Z was admitted as a partner. The profits for the year ended 31st December, 1946, amounted to £15,000, and on the latter date X retired.

Since the profits were increasing, it would obviously not be advantageous to the firm to claim a discontinuance on Z's admission during the 1945-46, as the assessment for 1944-45 and 1945-46 would be increased. Accordingly the assessments would be as follows :—

1944-45	On the previous year's profit	£6,000
1945-46	do.	£10,000
apportioned under Rule 9 as follows :—		

Firm of X and Y	$\frac{9}{12}$ ths	=	£7,500
„ „ X, Y and Z	$\frac{3}{12}$ ths	=	£2,500

On X's retirement in the year 1946-47, however, it would be advisable to claim, since the 1946-47 assessment of £50,000 would be discharged and the following substituted :—

On X, Y and Z	Actual	$\frac{9}{12}$ ths of £15,000	=	£11,250.
„ Y and Z	„	$\frac{3}{12}$ ths of the 1947 profits.		

An additional assessment would then be made on X, Y and Z for 1945-46 on the actual profits of their penultimate year (1st January to 5th April, 1946), i.e.,  $\frac{3}{12}$ ths of £15,000 = £3,750, less already assessed £2,500, net addition = £1,250. Under the above decision (*Osler v. Hall*), no additional assessment can be made on the original firm of X and Y, as it did not claim discontinuance. It will be observed therefore that the £50,000 never forms a basis of assessment. In other circumstances it might pay to claim on the first change and not on the second.

It is necessary to note that there is no continuity between a partnership and a limited company, even where the partners become the only members of that company, and, therefore, in every case where a business is converted into a limited company, it must be assessed as if discontinued and recommenced on the date of the succession.

In all cases where a business is assessed as discontinued under Rule 11, the rules for stock valuation apply as set out in § 9 (b) of this Chapter (§ 26—1938).

The date of the change of ownership of a business is a question of fact to be determined in each case on the exact circumstances. In general terms, the date of the vending<sup>1</sup> agreement must be taken to be the date of change, but if it can be shown that in fact the legal ownership passed on some other date, then that date is the date of change. The date mentioned in the agreement is not conclusive; the question is, when was there a succession *de facto* (*Todd v. Jones* (1930), 15 T.C. 396).

Whether or not there has been a “succession” to a business, is a question of fact. If the new owner acquires a trade and actually carries it on, there is a succession (see *Briton Ferry Steel Co. v. Barry* (1940), T.R. 39), but if the trade acquired is not carried on, *e.g.*, a wholesale trade is acquired by a retailer, who continues to retail but to do no wholesale trade, there is no succession (*Laycock v. Freeman, Hardy & Willis* (1938), 17 A.T.C. 451). In both cases, the vendor will be assessed on the discontinued business; if there is a succession, the purchaser will be assessed on the new business, but if there is no succession, the business acquired becomes merged in the existing business, which continues to be assessed on its preceding year’s profits. It is a question of fact for the Commissioners to decide whether or not it is true to say that the business in respect of which the successor is said to be making profits is the business to which he succeeded.

Where a barrister is appointed a King’s Counsel his profession is unchanged and he is not to be treated

as if he had discontinued one profession and commenced a new one (*Seldon v. Croom-Johnson and v. Thomas* (1932), 16 T.C. 740).

Where there is an absorption or amalgamation of businesses of a similar nature in such circumstances that it is considered to be a partnership change, the combined profits prior to the change must be looked at in ascertaining the assessments for the combined business.

#### Illustration.

A and B carried on business in partnership. On 1st January, 1946, they admitted C as a partner, C bringing in his own business. The profits for the year ended 31st December, 1945, were as follows :—A and B, £3,000; C, £600. The new firm of A B & C will be assessed for 1946-47 on the combined profits of £3,600. (In addition, one-fourth of the separate assessments for 1945-46 will be added together to arrive at the assessment on A B & C for the period from 1st January, 1946 to 5th April, 1946. The remaining three-fourths of A and B's 1945-46 assessment must be borne by A and B, and the three-fourths of C's assessment by C.)

If the new business is not of the same nature as that of the businesses amalgamated, it must be assessed as new.

Where a new branch is opened, it is a question of fact whether the new branch is to be considered as a mere development of the existing business, or the setting up of a new business to be assessed as such. In practice, multiple shops and other trades with more than one shop who open or close branches are normally regarded as merely expanding or contracting the one business.

Where a portion of an undertaking is discontinued, it will likewise depend upon whether it is a mere contraction of the business (in which case the assessment for the following year must be based upon the

profits of the whole undertaking in the year preceding the year of assessment), or whether a separate undertaking has been discontinued (in which case the parts will be separately assessed, that closed down being treated as discontinued). If, as a matter of fact, a company carries on two separate and distinct businesses, and one ceases, the assessment for the following year will be based upon the profits in the preceding year of the continuing business only.

The appointment of a receiver for debenture-holders does not create a succession. The assessments carry on as on a continuing business (*C.I.R. v. Thompson* (1936), 2 A.E.R. 651).

On a succession, neither unexhausted wear and tear allowances nor losses can be carried forward from the old business to the new (*United Steel Cos. v. Cullington* (1940), T.R. 195). On a "partnership" change, however, where the discontinued provisions are not claimed, the whole unexhausted wear and tear allowances can be carried forward and added to future wear and tear allowances of the firm, and each partner's share of loss can be carried forward against his share of profits in the usual way.

(b) *Concentration of Industry* (§ 18—1941).

Where, in connection with an arrangement for the concentration of industry, certified by or on behalf of the Board of Trade or other authorised Government Department as approved and in the national interest, having regard to the exigencies of the war, a person ceases to carry on all or any of his trade activities, or undertakes new activities in connection with his trade, the change is not to be regarded as the cessation or setting up of a trade.

Any sum payable under the arrangement to that person or his successor by another party to the arrangement (unless it is a capital payment or a sum from which income tax has properly been deducted), will be allowed as an expense of the payer and be regarded as a trade receipt of the payee. Any plant which remains unused as a result of any such arrangement will still rank for wear and tear allowance as if in normal use. "Person" here includes "partnership."

### § 11.—Partnership Assessments.

The assessment of a firm is a joint assessment made in the partnership name, and not separately on the individual partners constituting the firm (Sch. D, Cases I and II, R.10). This Rule is in effect an example of the principle of collection of tax at the source, and places the liability of paying the tax on the firm as a whole instead of making each partner directly liable for his proportion only.

The business is therefore the unit of assessment, *i.e.*, the source. As, however, the partners (provided they have made their Returns claiming them) are entitled to allowances, effect is given to the allowances in assessing the firm. It is therefore necessary to compute each partner's share of the firm's income in order to arrive at the allowances to which he is entitled. The total of the allowances of all the partners is then deducted in charging the partnership.

The method of profit-sharing agreed upon by the partners must be followed; if interest on capital and/or salaries have to be provided for in arriving at the share of profits, they must likewise be provided in dividing the statutory profits for Income Tax purposes.

It is therefore necessary to divide the assessment for the year of assessment between the partners in

the same manner as they would divide a profit of that amount *for that year*, irrespective of how they actually shared profits in the accounting year taken as the basis of the assessment or how much profit they make in the year of assessment (§ 20—1918).

In the case of continually fluctuating capital, it may be impossible to ascertain the interest on capital before the completion of the year of assessment, and the usual course is in the first place to take the interest of the previous year and to allocate the assessment accordingly, adjusting at a later date if necessary. A similar position may arise where the salary of a partner is changed during the year of assessment.

The precedent acting partner must make a return of the firm's profits, showing how the assessment is to be allocated according to the agreement for sharing profits in the year of assessment.

#### Illustration (1).

A, B & C are in partnership, sharing profits and losses equally. Their capitals vary from year to year, and interest at 5 per cent. per annum is allowed. They receive salaries as follows:—A £900, B £600, and C £300.

The following is the firm's Profit and Loss Account made up to the 31st December, 1945.

Dr.		PROFIT AND LOSS ACCOUNT.		Cr.
	£			£
To Trade Expenses (including E.P.T.) .. ..	1,628	By Gross Profits .. ..		13,182
„ Salaries .. ..	846			
„ Interest on Capital—				
A .. ..	850			
B .. ..	450			
C .. ..	150			
„ Partners' Salaries—				
A .. ..	900			
B .. ..	600			
C .. ..	300			
„ Depreciation of Lease ..	120			
„ Charitable Subscriptions ..	33			
„ Profit .. ..	7,810			
	<u>£13,182</u>			<u>£13,182</u>

The charitable subscriptions are not to institutions from which the employees might benefit and therefore are disallowed.



The interest on capital credited to the partners after 1st January, 1946, is A £950 ; B £500 ; and C £200, per annum.

#### INCOME TAX COMPUTATION.

Net Profits as per Accounts.	..	..	£7,310
<i>Add—</i>			
Interest on Capital—			
A	..	..	850
B	..	..	450
C	..	..	150
Partners' Salaries—			
A	..	..	900
B	..	..	600
C	..	..	300
Depreciation of Lease	..	..	120
Charitable Subscriptions	..	..	33
Adjusted profits			<u>£10,713</u>
Assessment, 1946-47			<u>£10,713</u>

Although based on the profit of the previous year, this sum is the assessment for 1946-47, and must be divided among the partners in the manner in which they divide profits for the year ending 5th April, 1947, irrespective of how they divided profits in the basic year 1945. Effect has to be given to the Interest and Salaries for 1946-47, not to those for 1945.

The Official Return Form requires the allocations to be set out as follows :—

Partner.	Salary.	Interest on Capital.	Basis of Distribution of Balance.	Amount of Partner's Share of Balance.
A .. ..	£900	£950	$\frac{1}{3}$ rd.	£2,421
B .. ..	600	500	$\frac{1}{3}$ rd.	2,421
C .. ..	300	200	$\frac{1}{3}$ rd.	2,421
	<u>£1,800</u>	<u>£1,650</u>		<u>£7,263</u>

Each partner will make his own Return claiming the allowances to which he is entitled, and effect will be given to these allowances in assessing the partnership. Assuming that A is married, with one child under 16; B is a widower, with one child

under 16 and a housekeeper, and C is single, and that the firm has no other income or annual charges, the tax payable would be allocated as follows :—

	Assessment on Firm, 1946-47.		Allocation—				
			A.		B.		C.
	£	£	£	£	£	£	£
		10,713		4,271		3,521	2,921
<i>Deduct Allowances—</i>							
Earned Income .. ..	450		150		150		150
Personal .. ..	400		130		110		110
Children .. ..	100		50		50		—
Housekeeper .. ..	50		—		50		—
		1,000		380		360	260
		<u>£9,713</u>		<u>£3,891</u>		<u>£3,161</u>	<u>£2,661</u>
<i>Chargeable—</i>							
at 3/- .. ..	£150	£22 10 0	£50	£7 10 0	£50	£7 10 0	£50
at 6/- .. ..	225	67 10 0	75	22 10 0	75	22 10 0	75
at 9/- .. ..	9,338	4,202 2 0	3,766	1,694 14 0	3,036	1,366 4 0	2,536
		<u>£4,292 2 0</u>		<u>£1,724 14 0</u>		<u>£1,396 4 0</u>	<u>£1,171 4 0</u>

The firm thus pays £4,292 2s. Od., of which £1,724 14s. Od. will be debited to A's current account, £1,396 4s. Od. to B's and £1,171 4s. Od. to C's. Each partner's private income will be chargeable at 9/- in the £, as he has already had the whole of his allowances.

The following is an illustration of a case where annual charges are paid partly out of the earned income of the firm :—

#### Illustration (2).

The firm of A, B and C made a profit in the year ended 31st January, 1946, as adjusted for tax purposes of £2,400. The Wear and Tear Allowance for 1946-47 was £300. Profits were shared in 1946-47 as follows: Interest on capital, A, £400; B, £200; C, £100; Salaries, B, £600; C, £1,000; Balance, A,  $\frac{2}{3}$ ths; B,  $\frac{2}{3}$ ths, and C,  $\frac{1}{3}$ th. The firm owned the business premises assessed at a net annual value of £500, and received income from investments (net) of £110 in 1946-47. Interest paid on loans was £1,000 (gross amount).

A was married, with no children eligible for relief; B was married with one such child; C was a bachelor. B's life was insured on a policy dated 1914 on which he paid a premium of £200; and C paid £120 a year on a policy dated 1932.

Show the tax payable by the firm, and the amounts to be charged to the partners for 1946-47.

Firm, 1946-47.		Allocation.		
		A.	B.	C.
Assessment, Sch. D ..	£ 2,100	£ 400	£ 200	£ 100
Interest on Capital			600	1000
Salaries .. ..			80	40
(a) Balance ..		320	720	1,060
Sch. A. . . £500				
Investment				
Income .. 200				
700				
Less Annual				
Interest 1,000				
(b) Excess	300	120	120	60
Statutory total				
income from firm		200	600	1,000
Deduct Allowances :				
(c) Earned Income .. £225		£25	£75	£125
(d) Personal .. .. 465		175	180	110
(e) Child .. .. 50		—	50	—
740		200	305	235
£1,360		—	£205	£765
Chargeable :				
at 3/- .. .. £100	£15 0 0		£50	£27 10 0
at 6/- .. .. 150	45 0 0		75	22 10 0
at 9/- .. .. 1,110	499 10 0		170	76 10 0
559 10 0			106 10 0	318 0 0
Less Life Assurance Relief at				
3/6 .. .. 38 10 0			(e)100 17 10 0	£120 21 0 0
Tax payable under Sch. D ..	521 0 0			
Sch. A £500 at 9/- ..	225 0 0			
By deduction, £200 at 9/- ..	90 0 0			
836 0 0				
Less recoupable from interest				
payable, £1,000 at 9/- ..	450 0 0			
Tax borne .. .. £386 0 0			£89 0 0	£297 0 0

NOTES.—(a) Since the total of the interest on capital and salaries exceeds the assessment by £200, that amount of “loss” is divisible in the profit-sharing ratio.

(b) The annual payments exceed the other income, leaving £300 payable out of earned income. To find the statutory total incomes of the partners this must be deducted in the profit-sharing ratio. It is not deductible from the firm’s assessment, however, as General Rule 19 requires it to be “kept in charge.”

(c) As has already been explained, the earned income allowance is restricted where charges are payable out of earned income, and is granted only on the income left to be enjoyed.

(d) A can only obtain relief for part of his allowances, as his income is exhausted thereby.

(e) B’s insurance premiums are limited to one-sixth of his total income.

(f) The firm pays in all £836 but recoups £450 thereof, leaving £386 to be borne. B and C are debited with £89 and £297 respectively.

(g) If any partner has private income, he can claim any balance of allowances against it, e.g., A has available £5 personal allowance, and the

whole of the reduced rate relief. If B has private income, his life assurance relief will be increased, as his premium has been limited to one-sixth of the total income, and if the total income exceeds £1,000 he will be entitled to the higher rate of relief.

An illustration will now be given of the computation of the tax payable and its allocation where the firm has other sources of income in excess of the annual charges and the partners have private incomes.

### Illustration (3).

A, B and C carried on business in partnership. For the year ended 30th November, 1945, the Profit and Loss Account was as follows:—

Dr.		PROFIT AND LOSS ACCOUNT.	Cr.
To Ground Rent .. ..	£ 40	By Gross Profit .. ..	£ 6,280
„ Rates and Insurance .. ..	200	„ Dividends (Gross amount) .. ..	200
„ Office Expenses .. ..	1,130	„ Bank Interest .. ..	10
„ Salaries .. ..	1,800		
„ Discounts .. ..	170		
„ Bad Debts written off .. ..	£60		
Less Transfer from .. ..			
Bad Debt Reserve .. ..	25		
	35		
„ Depreciation .. ..	265		
„ Amount written off Lease .. ..	90		
„ Interest on Loan B. .. ..	300		
„ Interest on Capital—			
A .. ..	£400		
B .. ..	200		
C .. ..	200		
	800		
„ Net Profit—			
A .. ..	£640		
B .. ..	640		
C .. ..	320		
	1,600		
	<u>£0,490</u>		<u>£0,490</u>

The salaries include £200 to C. The Bad Debt Reserve is adjusted each year to 5% of the debtors. The Net Annual Value of the premises (not a factory) for Income Tax, Schedule A is £155. The investments remain unchanged. It is agreed with the Inspector of Taxes that bank interest shall be left in charge in the Profit and Loss Account. The Wear and Tear Allowance for 1946-47 is agreed at £225.

As from 1st December, 1945, C's salary is increased to £300 per annum, and the capitals are varied, with the result that the interest for the year 1946-47 would be as follows:—

A—£500; B—£300; C—£300.

The balance of profits is divided as before. The interest payable on B's Loan to the firm remained constant.

A is a married man, with one child under 16. His wife owns the house in which they live (assessed under Schedule A at £80 per annum (net), subject to a mortgage of £700 at 5% per annum interest), and is the owner of a small business the adjusted profits of which for the year ended 31st December, 1945, amounted to £420. A pays a premium of £60 per annum on an assurance policy on his own life, taken out in 1912.

B is single and wholly maintains his widowed mother, but has no income other than that from the partnership.

C is a widower, whose sister lives with him as housekeeper. He holds £2,857 3½% War Loan, and pays a premium of £48 per annum on a policy on his own life taken out on 1st July, 1946, the premium being payable by monthly instalments of £4.

#### INCOME TAX COMPUTATION, 1946-47.

Net Profit per Accounts	..	..	£1,600
<i>Add—</i>			
Ground Rent	..	..	40
C's Salary	..	..	200
Depreciation	..	..	265
Amount written off Lease	..	..	90
Interest on Loan B	..	..	300
Interest on Capital	..	..	800
			<hr/>
			£3,295
<i>Deduct—</i>			
Bad Debt Reserve	..	..	£25
Dividends	..	..	200
Net Annual Value of Premises	..	..	155
			<hr/>
			380
			<hr/>
Adjusted profits	..	..	£2,915
			<hr/>
Sch. D, Case I, Previous year's profits			£2,915
Less Wear and Tear Allowance			225
			<hr/>
Assessment, 1946-47	..	..	£2,690
			<hr/>
Schedule A Assessment	..	..	£155

The firm has also income taxed at source, dividends £200, and pays Annual Charges: ground rent £40, and interest on loan £300, from both of which Income Tax must be deducted at source.

NOTES.—(1) The majority of the adjustments have already been fully explained in earlier examples.

(2) Interest on loans as distinct from capital is an annual payment from which tax is deductible under General Rule 19.

(3) Since the bad debt reserve is not against specific debts, the appropriation would not have been allowed as a deduction for Income Tax purposes when made, and has therefore borne tax. The £25 brought into credit in the Profit and Loss Account is not again subject to tax and must be eliminated.

## ALLOCATION OF ASSESSMENT, 1946-47

	Salary.	Interest on Capital.	Basis of Distribution of Balance.	Amount of Partner's Share of Balance.	Total.
A ..	—	£500	$\frac{2}{5}$ ths.	£516	£1,016
B ..	—	300	$\frac{2}{5}$ ths.	516	816
C ..	£300	300	$\frac{1}{5}$ th.	258	858
	<u>£300</u>	<u>£1,100</u>		<u>£1,290</u>	<u>£2,690</u>

## FIRM'S COMPUTATIONS, 1946-47.

				Firm.	A.	Allocated to		C.
Partnership Profits .. ..				£2,690	£1,016	£816		£858
<i>Deduct Allowances:</i>								
Earned Income .. .. £336					£127	£102		£107
Personal .. .. 400					180	110		110
Child .. .. 50					50			
Dependent Relative .. .. 50						50		
Housekeeper .. .. 50							50	
				886	357	262		267
				<u>£1,804</u>	<u>£659</u>	<u>£554</u>		<u>£591</u>
Chargeable				£ s. d.	£ s. d.	£ s. d.		£ s. d.
at 3/- .. .. £150				22 10 0	£50 7 10 0	£50 7 10 0	£50	7 10 0
at 6/- .. .. 225				67 10 0	75 22 10 0	75 22 10 0	75	22 10 0
at 9/- .. .. 1,429				943 1 0	584 240 6 0	429 193 1 0	406	209 14 0
				738 1 0	270 6 0	223 1 0		239 14 0
<i>Less Life Assurance Allowances—</i>								
at 5s. 8d. .. .. £60 .. £15 15 0					£60 15 15 0			
at 3s. 6d. .. .. £40 .. 7 0 0							£40	7 0 0
				22 15 0				
Tax payable under Sch. D, Case I ..				710 6 0	254 11 0	223 1 0		232 14 0
Tax payable under Sch. A at 9/- .. £155				89 15 0				
Tax suffered by deduction from Dividends at 9/- .. .. 200				90 0 0				
				£355	870 1 0			
<i>Less Recouped from Annual Charges—</i>								
Ground Rent .. .. £40								
Interest on Loan .. .. 300								
				£340	153 0 0			
Excess of unearned income over charges .. £15					£6 2 14 0	£6 2 14 0	£3	1 7 0
To be charged to partners .. ..				£717 1 0	£257 5 0	£225 15 0		£234 1 0

NOTE.—No assessments are made on the individual partners but simply on the firm. The "allocation" columns, however, have been added here in order to show clearly the method of arriving at the amounts to be charged to the Current Accounts of the partners.

## PRIVATE COMPUTATIONS, 1946-47.

	A.	B.	C.
Wife's Business .. ..	£420		War Loan Interest.
Deduct Allowances—			Sch. D
Earned Income ..	£28		Case III
Additional Personal ..	110		£100 at 9/-
	<u>183</u>		<u>£45 0 0</u>
	<u>£287</u>		
£287 at 9/- .. ..	<u>£129 3 0</u>		
House—Sch. A.			
£80 at 9/- .. ..	£36 0 0		
Tax recouped from Mortgage Interest:			
£35 at 9/- .. ..	15 15 0		
Tax borne.. ..	<u>£20 5 0</u>	Tax borne by deduction from Loan Interest, £300 at 9/-	<u>£135 0 0</u>

## TOTAL TAX BORNE.

	Firm.	A.	B.	C.
	£ s. d.	£ s. d.	£ s. d.	£ s. d.
Through Firm .. ..	<u>£717 1 0</u>	257 5 0	225 15 0	234 1 0
Sch. D Case I (Wife) .. ..		129 3 0		
III .. ..				45 0 0
Sch. A less charge .. ..		20 5 0		
By Deduction .. ..			135 0 0	
		<u>£406 13 0</u>	<u>£360 15 0</u>	<u>£279 1 0</u>

NOTES.—(1) In order to arrive at the partners' shares of the firm's Statutory Total Income, the Income from other sources and the Annual Charges must be divided among the partners in their profit sharing ratio, i.e., 2 : 2 : 1. This is best done as shown by dividing only the excess.

(2) The allowances applicable to private income, i.e., on the business of Mrs. A, are deducted from such income.

(3) Care must be taken to arrive at the Statutory Total Income of each individual for Life Assurance Allowance purposes. A's Total Income is over £1,000, but not over £2,000, hence the insurance relief is computed at three-quarters of the standard rate, the policy being dated prior to 23rd June, 1916.

C has paid only ten months' premiums during the year, and his relief is accordingly on £40.

PROOF.				A.	B.	C.
				£	£	£
Income from Firm—						
Earned	..	..	..	1,016	816	858
Unearned	..	..	..	142	142	71
				<u>1,158</u>	<u>958</u>	<u>929</u>
Less Charges	..	..	..	136	136	68
Statutory Total Income from Firm	..	..	..	1,022	822	861
Wife's Business	..	..	..	420		
Sch. A	..	..	..	80		
Sch. D, Case III	..	..	..			100
Loan Interest	..	..	..		300	
				<u>1,522</u>		
Less Mortgage Interest	..	..	..	35		
Statutory Total Income from all Sources				1,487	1,122	961
Deduct Allowances—						
Earned Income	..	..	£150	£102	£107	
Personal	..	..	180	110	110	
Additional Personal	..	..	110			
Child	..	..	50			
Dependent Relative	..	..		50		
Housekeeper	..	..			50	
				<u>400</u>	<u>262</u>	<u>267</u>
				<u>£997</u>	<u>£860</u>	<u>£694</u>
				£ s. d.	£ s. d.	£ s. d.
£50 at 3/- ; £75 at 6/-	..	..	£125 30 0 0	£125 30 0 0	£125 30 0 0	30 0 0
At 9/-	..	..	872 392 8 0	735 330 15 0	569	256 1 0
			<u>422 8 0</u>	<u>360 15 0</u>		<u>286 1 0</u>
Less Life Assurance Allowance—£60 at					£40 at	
5s. 8d.			15 15 0		3s. 6d.	7 0 0
Tax to be borne	..	..	<u>£406 13 0</u>	<u>£360 15 0</u>		<u>£279 1 0</u>

The following is an illustration of the division of the assessment where there has been a change in the partners :—

#### Illustration (4).

L, K and H were in partnership, sharing profits equally, after charging interest on capital at 5%. On 30th June, 1946, K died. No claim was made under Rule 11 to be assessed as discontinued and recommenced.

The capitals had been fixed at £10,000, £5,000 and £5,000 respectively. On K's death, however, the capitals of L and H were adjusted to £12,000 each, and L thereafter received a salary of £600 per annum, payable monthly.

The adjusted profits for the year ended 30th June, 1945, were £8,000. Show the division of the 1946-47 assessment.



The assessment is first "split" under Rule 9 :—

Assessment for 1946-47 .. £8,000.

Proportion, 6th April, 1946, to 30th June, 1946, say  $\frac{3}{12}$ ths  
of £8,000 = £2,000.

Proportion 1st July, 1946, to 5th April, 1947, say  $\frac{9}{12}$ ths  
of £8,000 = £6,000.

The assessment is then divided—

	L.			K.			H.		
	£	s.	d.	£	s.	d.	£	s.	d.
To June 30th, 1946 :—									
Interest on Capital (5% for three months) ..	125	0	0	62	10	0	62	10	0
Balance £(2,000—250) equally .. .. .	583	6	8	583	6	8	583	6	8
From June 30th, 1946 :—									
Interest on Capital (5% for nine months on new capitals) .. .. .	450	0	0				450	0	0
Salary, nine months .. .. .	450	0	0						
Balance £(6,000—1,350) equally .. .. .	2,325	0	0				2,325	0	0
	£ 3,933 6 8			£645 16 8			£3,420 16 8		

*Note to Illustration.*

The assessment of £8,000 being, from an Income Tax point of view, the profit of the year ended 5th April, 1947, must be divided among the partners as they share profits in that year. The proportion of the assessment relating to the period from 6th April to 30th June is therefore divided according to the old agreement, and the balance according to the new agreement.

Since it is the partnership business that is being assessed, no account of private incomes of the partners can be taken for the purposes of General Rules 19 and 21. If, therefore, the annual charges of the firm exceed its income from all sources, a Rule 21 assessment must arise, irrespective of the fact that the partners may have private incomes greatly in excess thereof. Where there is an excess of private charges over private income, however, the excess will be taken into account in charging the firm, in so far as it affects the allowances of the individual partners. As to the position of partnerships where a loss arises, see Chapter VII.

**§ 12.—Distribution of Income Tax over the Profits of a Limited Company.**

The authority for the deduction of tax from dividends is contained in Gen. Rule 20 as amplified by § 7—1931 and § 20—1940. Gen. Rule 20 reads :—

“The profits or gains to be charged on any body of persons shall be computed in accordance with the provisions of this Act on the full amount of the same before any dividend thereof is made in respect of any share, right or title thereto, and the body of persons paying such dividend shall be entitled to deduct the tax appropriate thereto.”

The rule must be construed as authorising the company to deduct tax from any dividend paid—

- (a) Out of a balance of profits which have been charged to tax ; or
- (b) Out of the profits of the current year, if those profits would, if tax were chargeable on a current year basis, be taken into account in computing the liability to tax (§ 7—1931).

In order to cover cases where the company pays the dividend “free of tax,” or does not deduct tax, or deducts less than the standard rate, it is provided that, to the extent to which a dividend is paid out of profits (as explained in the preceding paragraph), the sum paid is to be regarded as representing income of such an amount, as, after deduction of tax, would equal the net amount paid (§ 20—1940). The principle involved seems to be that all undistributed profits belong to the ordinary shareholders and any under or over deduction is not really material.

This does not apply to a preference dividend (*i.e.*, a dividend payable on a preferred share at a fixed rate only, or such part of a dividend payable on a preferred

share as is payable at a fixed gross rate only) (§ 7—1931), except where either no tax has been deducted or tax has been deducted at less than the standard rate (unless the under-deduction is due solely to a change in the standard rate) (§ 20—1940).

The rate at which tax is deductible is the standard rate for the year in which the amount payable becomes due (§ 39—1927); a dividend is deemed to be due on the date on which it is declared payable (*Hurll v. C.I.R.* (1922), 8 T.C. 293; *Duncan v. C.I.R.* (1923), 8 T.C. 433).

As to the rate of tax deductible from dividends where the company has received any Dominion Income Tax Relief (see Chap. X).

Every warrant, cheque, etc., issued in payment of any dividend or interest distributed by any company within the meaning of the Companies Act, 1929, or a company created by letters patent or by or in pursuance of an Act of Parliament, must (under penalty) be accompanied by a statement in writing showing—

(a) the gross amount which, after deduction of the Income Tax appropriate thereto, corresponds to the net amount actually paid; and

(b) the rate and the amount of Income Tax appropriate to such gross amount; and

(c) the net amount actually paid (§ 33—1924).

The section does not apply to a company registered abroad, even if it is controlled in this country and charged on the whole of its profits.

If the company declares a dividend expressed to be “free of tax,” the effect is to declare a dividend at a higher rate, i.e., a dividend of 5% “free of tax” is equivalent to a dividend of  $9\frac{1}{11}$  less tax at 9/- in the £.

Where a dividend was paid out of a fund which was not liable to tax (e.g., capital profits), it was held that it could not be made to suffer tax by deduction, nor was such dividend assessable in the hands of the recipients (*Gimson v. C.I.R.* (1930), 99 L.J.K.B. 532).

The C.I.R. regard interest on tax reserve certificates as applied in paying the tax, thereby releasing an equivalent amount of profits for dividends. Accordingly, such interest cannot be regarded as a fund available for a dividend under the *Gimson* rule; if a dividend is paid out of such interest, it will be regarded as a net dividend of the amount of its gross equivalent. This has been upheld, on appeal, by the Special Commissioners.

From the above remarks, it will be seen that a company may deduct tax from a dividend, either expressly or by declaring the dividend "free of tax," even where it has no liability to pay tax for the year, so long as its current profits are sufficient. Any shareholder receiving a dividend in such a case is in receipt of income which has suffered tax by deduction, and he can claim repayment from the Revenue in respect of any allowances to which he is entitled.

There is no analogy between Rule 20 and Rule 21 of the General Rules in this respect. The company is entitled to deduct tax on the dividend to the extent that the dividend does not exceed the total of its assessments (other than those under General Rule 21), plus income taxed at source, or the total of its adjusted profits for that year plus its other income of that year, whichever total is the greater (§ 7—1931). It is thought that any dividend which exceeds the higher of these totals ought to be paid gross, as no deduction is authorised by Gen. Rule 20; it could not be assessed on the recipient as there is no charging provision in the Acts.

### § 13.—Rate for deduction of tax where the Standard Rate is altered.

Since the Budget Resolution under the Provisional Collection of Taxes Act, 1913 (*see* Chap. I) is not

(iv) Rents on long leases and certain other payments charged on property chargeable under Sch. A (*e.g.*, rent charges).

Any under-deduction arising by reason of the change in the standard rate is, so far as possible, to be made good by increasing the deduction from the next payment, and if necessary from subsequent payments made before 1st September, of the following year, such tax to be accounted for in the usual way. Where, however, there is no such subsequent payment from which the adjusting deduction can be made, Bankers, Agents or other persons who have made payments falling within this Class since 5th April, and have under-deducted tax, will be required to furnish to the Commissioners of Inland Revenue lists containing the names and addresses of the persons to whom the payments have been made and the amounts of such payments.

Any under-deduction is assessed under Case VI on the recipient of the income.

Any over-deduction is made good by the Revenue in practice (§ 211—1918 ; § 12—1930 ; 5th Sch.—(No. 2) 1940).

**Class II.** *Payments made out of profits or gains brought into charge to tax.*

- (a) Preference dividends (*see* definition below).
- (b) Items enumerated in (d) of Class I where paid out of profits or gains brought into charge to tax.

Where tax has been deducted from payments falling within this class by reference to the old rate, the payer is to adjust the under-deduction or over-deduction by making a corresponding extra or smaller deduction (as the case may be) from the next subsequent like payment. If there is no such further payment from which an adjusting deduction can be made, the payer is entitled to recover the amount under-deducted directly from the recipient of the payment from which the insufficient deduction was made and must account within one year for any over-deduction to the person entitled to the securities at the date of adjustment (§ 211—1918 ; § 12—1930 ; 5th Sch.—(No. 2) 1940).

The expression “ preference dividend,” as used above means—

- (a) a dividend payable on a preferred share at a fixed gross rate per cent. ; or
- (b) where a dividend is payable on a preferred share partly at a fixed gross rate per cent, and partly at a variable rate, such part of that dividend as is payable at a fixed gross rate per cent., and the expression “ share ” includes stock (§ 12 (4)—1930).

**Class III.**

Ordinary dividends.

The Income Tax Acts do not authorise any subsequent adjustment in respect of under or over-deductions of tax from such

payments, but provide (§ 12 (3)—1930) that where on payment of a dividend (other than a preference dividend as defined above), Income Tax has been deducted by reference to a standard rate of tax greater or less than the standard rate for the year in which the dividend became due, the net amount received must be deemed to represent a gross dividend of such amount as after deduction of the new rate of tax would leave the net dividend received (§ 12—1930).

The rules are clearly summarised in the Report of the Income Tax Codification Committee as follows :—

ADJUSTMENTS NECESSITATED BY CHANGE OF RATE.

Nature of Payment.	Increase in Rate.	Decrease in Rate
<b>A. Payments made out of profits or gains brought into charge to tax.</b>		
(1) Dividends under General R. 20 :—		
(a) Ordinary dividends.	1930, S. 12 (3); No provision for adjustment.	1930, S. 12 (3); No provision for adjustment of deductions as such.
(b) Preference dividends.	1918, S. 211 (2); applied by 1930, S. 12 (2); Adjusted on next payment.	1930, S. 12 (1), Adjusted on next payment if over-deduction not already made good otherwise.†
(2) Other payments :—		
(a) Interest payable under General R. 19 :—		
(i) by body corporate (including interest paid out of rates which is charged to tax under Sch. D, Misc. R. 6);	1918, S. 211 (2); Adjusted on next payment.	1930, S. 12 (1); Adjusted on next payment if over-deduction not already made good otherwise.
(ii) by individual or unincorporate body.	1918, S. 211 (2); Adjusted on next payment.	1913, S. 2; Payer liable to make good to payee.
(b) Annuities	1918, S. 211 (2); Adjusted on next payment.	1913, S. 2; Payer liable to make good to payee.
(c) Patent royalties and mineral royalties to which General R. 19 applies	1918, S. 211 (2); applied by 1930, S. 12 (2); Adjusted on next payment (mineral royalties brought in by 1934, S. 21)	1913, S. 2; Payer liable to make good to payee.
(d) Payments falling within Sch. A, No. VIII, R. 4.	1918, S. 211 (2); Adjusted on next payment.	1918, S. 2; Payer liable to make good to payee.
<b>B. Payments not made out of profits or gains brought into charge to tax.</b>		
(1) Sch. C & Sch. D, Misc. R. 7	1918, S. 211 (1); Lists obtained from payers; assessments made on recipient under Case VI.	1913, S. 2; Repayment or adjustment is in practice made by the Revenue.
(2) General R. 21 (including patent and mineral royalties, and copyright royalties paid to persons abroad).	1918, S. 211 (2); Adjusted on next payment. Patent royalties brought in by 1930, S. 12, and mineral royalties by 1934, S. 21.	1918, S. 2; Repayment or adjustment is in practice made by the Revenue.

† Retention by the company of the amount over-deducted is not in any case authorised for more than one year after the passing of the Finance Act.

**Illustrations.**

(1) On 12th April, 1940, B Ltd., declared and paid a dividend for the half-year ended 31st March, 1940, upon its 6% Preference Shares. The increase in the Standard Rate from 7s. 6d. to 8s. 6d. was not then known, and Income Tax was accordingly deducted at 7s. 6d. In paying the dividend to 30th September, 1940, the company had therefore to deduct tax at 9s. 6d. in the £, being 8s. 6d. plus 1s. 0d. under-deducted in April.

If a shareholder in the meantime had sold his shares, the new holder would suffer the additional deduction, but this should be taken into account in fixing the transfer price of the shares.

(2) On 12th April, 1940, B Ltd., also declared and paid a dividend of 12% upon its Ordinary Shares. X, the holder of 1,000 £1 shares, therefore received a dividend made up as follows:—

	£	s.	d.
12% on 1,000 shares of £1 each .. ..	120	0	0
<i>Less</i> Income Tax at 7s. 6d. in £ .. ..	45	0	0
Net amount .. .. .	<u>£75</u>	<u>0</u>	<u>0</u>

X must include in his Return this net amount grossed up as if it had suffered tax at 8s. 6d. in the £, i.e., as if it were a gross dividend of

$£75 \times \frac{20s.}{11/6d.} =$ .. .. .	£130	8	8
<i>Less</i> tax at 8s. 6d. in £ .. .. .	55	8	8
	<u>£75</u>	<u>0</u>	<u>0</u>

If X is exempt from tax by reason of allowances, he can reclaim £55 8s. 8d. although only £45 was deducted. (On the other hand, if he is a Sur-tax payer, he will pay Sur-tax on the excess.)

(3) On 20th April, 1940, A paid Interest on Loan amounting to £200, at the same time repaying half the loan.

In order to adjust the under-deduction of Income Tax when making the half-yearly payment on 20th October, 1940, A must deduct tax as follows:—

	£ s. d.	£ s. d.
Interest for half-year .. ..		100 0 0
Less Income Tax at 8s. 6d. thereon	42 10 0	
do. 1s. 0d. on £200		
paid 20th April, 1940, to bring		
rate up from 7s. 6d. to 8s. 6d.	10 0 0	
	<hr/>	52 10 0
Net		<hr/> £47 10 0 <hr/>

(The actual rate deducted on the second payment is  $\pounds \frac{52.5}{100} = 10\text{s. } 6\text{d.}$ , owing to the alteration in the interest itself.)

## § 14.—Reserves for Income Tax.

### (a) Private Firms.

Owing to the high rate of tax, partnerships sometimes decide to make a reserve for the Income Tax payable before dividing profits. This presents some difficulties, owing to the allowances of the individual partners, but the reserve can in most cases be estimated with sufficient accuracy. Each Partner's Current Account should be debited with the appropriate part of the reserve applicable to him, the total reserve being credited to the Income Tax Account and carried forward. When the tax is paid, it should be debited to Income Tax Account.

On any alteration in the shares of the partners or in the constitution of the firm, any balance standing to the credit of the Income Tax Reserve Account should be written back to the Partners' Accounts, on the basis on which it was credited.

It is perhaps more usual, however, not to create any separate Reserve Account, but to compute the amount which each partner must leave on Current



Account to meet his share of the firm's income tax liability, restricting cash drawings accordingly.

In any accounting period, the tax up to 5th April in the period will normally have been paid. It is therefore necessary to reserve at least for the accrued proportion of the current year's tax from 5th April to the date of the accounts, *e.g.*, if accounts are made up for the year to 31st December, three-quarters of the current year of assessment has elapsed, and that proportion of the tax payable on assessments should be reserved. If the accounting period ends before 1st July, however, the second instalment due on that date must also be taken into account.

When making reserves for Income Tax, it should particularly be remembered that the reserve should be provided only in respect of amounts upon which the concern itself is liable to bear tax. Thus, so far as Income Tax has been suffered by deduction at source or is recoupable by deduction from charges under General Rule 19, a reserve is not necessary. A reserve must be made for Income Tax deducted under General Rule 21, but not yet paid over.

The whole point to consider is not what Income Tax a firm will pay, but what amount must be reserved for, in respect of their own profits.

Many firms like to go further and reserve for the estimated tax payable for the year in which the accounts form the basis of assessment. This is discussed in (b) below. In the following illustration, only the accrued liability is considered; once the principles are grasped, their application to other circumstances is a matter of detail.

**Illustration.**

A. & F. Jones started business on the 1st January, 1946. They share profits and losses equally, and introduce an equal amount of capital, viz., £10,000 each. A. Jones is married, with one child under 16; F. Jones is single. Neither has any other income.

They desire a reserve to be made in respect of Income Tax, and submit the following Profit and Loss Account showing the result of their first year's trading. All charges are payable quarterly on 31st March, 30th June, 30th September, and 31st December.

Show (1) The Appropriation Account, (2) The Current Accounts, (3) The Income Tax Account, and (4) The Royalties Account.

Ignore Schedule A tax, being wholly deductible from rent.

**A. & F. JONES.****PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED**

<i>Dr.</i>		31st DECEMBER, 1946.		<i>Cr.</i>	
		£	s. d.		£ s. d.
To Trade Expenses ..	1,100	0	0	By Gross Profit ..	10,810 0 0
„ Salaries ..	2,400	0	0		
„ Royalties on Patents ..	500	0	0		
„ Rent ..	500	0	0		
„ Rates ..	80	0	0		
„ Annuities ..	100	0	0		
„ Interest on Loans ..	200	0	0		
„ Repairs to Premises ..	80	0	0		
„ Interest on Capital ..	1,000	0	0		
„ Balance, Net Profit ..	4,840	0	0		
		<u>£10,810</u>	<u>0 0</u>		<u>£10,810 0 0</u>

**INCOME TAX COMPUTATION.**

Net Profit .. .. .	£4,840
Add Royalties .. .. .	500
Annuities .. .. .	100
Interest on Loans .. ..	200
Interest on Capital .. ..	1,000
Adjusted profit .. .. .	<u>£6,640</u>

**Assessments :—**

1945-46—Actual Profits  $\frac{1}{2}$ ths of £6,640 = £1,660.

1946-47—Profits of first 12 months = £6,640.

Since the capitals are equal, and no salaries are payable, these assessments are divisible equally.

Computation of tax payable:—

		1945-46.		1946-47.	
		A. Jones.	F. Jones	A. Jones.	F. Jones.
Shares of Assessment ..		£830	£830	£3,320	£3,320
<i>Deduct: Annual Charges—</i>					
Royalties ..	£500				
Annuities ..	100				
Interest on Loans	200				
	£800 (a)	100	100	400	400
		730	730	2,920	2,920
<i>Deduct: Allowances—</i>					
Earned Income ..	£73 (b)	73		150	150
Personal ..	140	80		180	110
Child ..	50			50	
		263	153	380	260
Taxable Incomes		£467	£577	£2,540	£2,660
Chargeable: at 6s. 6d. ..	(£165) 53 12 6	(£165) 53 12 6	at 3/- (£50) £7 10 0	(£50) £7 10 0	at 3/- (£50) £7 10 0
at 10/- ..	(802) 151 0 0	(412) 206 0 0	at 6/- (75) 22 10 0	(75) 22 10 0	at 6/- (75) 22 10 0
			at 9/- (2,415) 1,086 15 0	(2,535) 1,140 15 0	at 9/- (2,415) 1,086 15 0
	£204 12 6	£259 12 6	£1,116 15 0	£1,170 15 0	
Tax to be borne by firm ..		£464 5 0	£2,287 10 0		

NOTE.—The Tax to be borne by the firm excludes the tax deductible from the annual charges. Such tax will have to be paid over to the Revenue Authorities (as part of the assessment) and will be taken into account in ascertaining the total reserve for Income Tax.

		1945-46.		1946-47.	
<i>Proof.—Assessment on Firm ..</i>		£1,660		£6,640	
<i>Less Allowances ..</i>		416		640	
		£1,244		£6,000	
Chargeable—					
at 6s. 6d. ..	£330	£107 5 0	at 3/- £100	£15 0 0	
at 10/- ..	914	457 0 0	at 6/- 150	45 0 0	
			at 9/- 5,750	2,587 10 0	
Tax payable ..		564 5 0		2,617 10 0	
<i>Less recouped from charges,</i>					
£200 at 10/- ..	100	0 0	£800 at 9/-	360 0 0	
Tax to be borne ..	£464	5 0		£2,287 10 0	

Notes.—

(a) The charges are those payable in the year of assessment.

(b) Where charges are paid out of earned income, the earned income allowance is given only on the statutory income, since this is less than the earned income, and allowance cannot be granted on an amount which is being paid over to some other person.



Dr.		ROYALTIES ACCOUNT.				Cr.	
		£	s.	d.			
1946.					1946.		
Mar. 31	To Cash—Royalty less Tax				Dec. 31	By P. & L. Account ..	
	at 10/- .. ..	62	10	0		£	
June 30	.. do. at 9/- .. ..	68	15	0		500	
Sept. 30	.. do. .. ..	68	15	0		0	
Dec. 31	.. do. .. ..	68	15	0		0	
	.. Income Tax Account	231	5	0			
		<u>£500</u>	<u>0</u>	<u>0</u>		<u>£500</u>	
						<u>0</u>	
						<u>0</u>	

*Notes to Illustration.*

(1) Tax on royalties on patents, annuity and loan interest should be deducted at the time of payment (General Rule 19).

(2) As this Firm commenced business on the 1st January, 1946, they will be liable to tax for the period from 1st January, 1946, to 5th April, 1946, in respect of the fiscal year 1945-46. It is usual to keep the matter of the first assessment open until the first accounts are available. Strictly, the tax for 1945-46 should be paid on 1st January, 1946, and 1st July, 1946, and that for 1946-47 on 1st January, 1947, and 1st July, 1947, but in practice this also would be kept open until the accounts were available and the proper assessment made. Only three-quarters of the 1946-47 tax is reserved for, since the assessment relates to the year from 6th April, 1946, to 5th April, 1947, and only a period of nine months of this year falls into the accounting year ended 31st December, 1946.

When the Income Tax for 1945-46 and 1946-47 (amounting to £564 5s. 0d. + £2,647 10s. 0d. = £3,211 15s. 0d.) has been paid, the balance on the Income Tax Account in respect of the period to 5th April, 1947, would be made up as follows:—

	£	s. d.
Income Tax paid .. .. .	3,211	15 0
Less Reserve brought forward .. ..	£2,549	17 6
Tax deducted on 31st March—		
Annuity .. ..	£25	
Interest .. ..	50	
Royalties .. ..	125	
	<u>£200</u>	<u>at 9/-</u>
		90 0 0
		2,639 17 6
		<u>£571 17 6</u>

Equal to the tax to be borne by the partners for the quarter, viz.:—

A. Jones, $\frac{1}{4}$ th of £1,116 15s. 0d. .. ..	=	£279 3 9
F. Jones, $\frac{1}{4}$ th of £1,170 15s. 0d. .. ..	=	292 13 9
		<u>£571 17 6</u>

If the more prudent method is adopted of reserving for tax payable in respect of the profits where they will form the basis of assessment (as explained in (b) below), in addition to all tax to the 5th April following the date of the accounts, it would be necessary to charge against the partners the estimated tax for 1947-48, as well as the odd quarter of 1946-47. This would be too great a burden for the one year, and as is the case where a change is made from the "minimum legal" basis to the ideal, it is usually necessary to build up the reserve over a period of years.

**(b) Limited Companies.**

In the case of limited companies, it was at one time the general practice to reserve only for the accrued liability to the date of the balance sheet, *i.e.*, for the proportion to the date of the accounts of the tax payable for the year of assessment.

Some companies, however, reserved for the full liability on the assessment for the year in which the accounts ended; others for the legal liability, or for tax on the actual profits, whichever sum was higher, in order that there might be reserved sufficient to pay the Income Tax on the assessment based upon such profits in the following year, when profits might be lower.

In general, however, companies now reserve most conservatively by providing for all tax assessed plus tax on the profits for the accounting year, and debit all dividends to the Profit and Loss Appropriation Account *net*, taking no credit to Income Tax Account for Income Tax deducted therefrom. This follows the recommendations of the Institute of Chartered Accountants in England and Wales, set out *post*.

The tax provided up to 5th April following the date of the Balance Sheet will appear in the Balance Sheet as a current liability; that for the following year of assessment (based on the accounts under review) as a reserve.

The following illustration shows the position under (1) the minimum "legal" method and (2) the method recommended by the Institute of Chartered Accountants, which provides for the tax on the whole profits.

**Illustration.**

Company commenced business 1st January, 1942, and made up its accounts to 31st December in each year. For the purposes of the illustration, Income Tax is assumed to continue at 10/- in the £. E.P.T. is ignored, as its introduction would vitiate the lessons to be demonstrated.

Year	1942	1943	1944	1945	1946	1947	1948	1949	1950	1951
Profits	£4,000	£7,000	£11,000	£20,000	£12,000	£5,000	£1,000	£100	£10,000	£20,000
Year of Assessment	1941/42	1942/43	1943/44	1944/45	1945/46	1946/47	1947/48	1948/49	1949/50	1950/51
	1951/52									
Assessment	£1,000	£4,000	£4,000	£7,000	£11,000	£20,000	£12,000	£5,000	£1,000	£10,000
Tax	£500	£2,000	£2,000	£3,500	£5,500	£10,000	£6,000	£2,500	£500	£5,000
(1) Minimum "Legal" Basis										
Year to Dec. 31	Tax paid in year	Dr. Profit and Loss Account				Reserve in Balance Sheet	(2) Institute recommendations			
							Dr. Profit and Loss Account	In Balance Sheet	Provision	Reserve
1942	—	$£500 + \frac{1}{2} \times £2,000 = £2,000$				£2,000	£4,500	£2,500	£2,500	£2,000
1943	£2,500	$\frac{1}{2} \times £2,000 + \frac{1}{2} \times £2,000 = £2,000$				£1,500	£3,500 8,000	£2,000	£3,500	£3,500
1944	£2,000 4,500	$\frac{1}{2} \times £2,000 + \frac{1}{2} \times £3,500 = £3,125$				£3,025	£5,500 13,500	£3,500	£5,500	£5,500
1945	£3,500 8,000	$\frac{1}{2} \times £3,500 + \frac{1}{2} \times £5,500 = £4,500$				£4,125	£10,000 23,500	£5,500	£10,000	£10,000
1946	£5,500 13,500	$\frac{1}{2} \times £5,500 + \frac{1}{2} \times £10,000 = £7,750$				£7,500	£6,000 29,500	£10,000	£6,000	£6,000
1947	£10,000 23,500	$\frac{1}{2} \times £10,000 + \frac{1}{2} \times £6,000 = £7,000$				£4,500	£2,500 32,000	£6,000	£2,500	£2,500
1948	£6,000 29,500	$\frac{1}{2} \times £6,000 + \frac{1}{2} \times £2,500 = £3,875$				£1,875	£500 32,500	£2,500	£500	£500
1949	£2,500 32,000	$\frac{1}{2} \times £2,500 + \frac{1}{2} \times £500 = £1,000$				£375	£50 32,550	£500	£50	£50
1950	£500 32,500	$\frac{1}{2} \times £500 + \frac{1}{2} \times £50 = £163$				£38	£5,000 37,550	£50	£5,000	£5,000
1951	£50 32,550	$\frac{1}{2} \times £50 + \frac{1}{2} \times £5,000 = £2,525$				£2,750	£10,000 47,550	£5,000	£10,000	£10,000

It will be seen that under method (1), when profits drop, as in 1946, 1947, 1948, and 1949, the amount of income tax to be debited to Profit and Loss Account may exceed the profits. If profits have been distributed up to the hilt, the company may have great difficulty in meeting the tax liability. Under method (2), each year (after the first) is charged with tax on its own profits, irrespective of the year in which that tax will fall due. The building up of the reserve in its initial stages could not, of course, be provided all in one year as has been done for emphasis above; it would have to be spread over a number of years. The Institute method has provided more than tax on the profits (owing to provision not only for the liability to date and on current profits, but also for the liability from the date of the accounts to the following 5th April), but has avoided any difficulty in any year (subject to the above spread). The position in 1942 shows clearly that this "over-provision" is essential to provide for all contingencies, by providing out of rising profits the tax that will be payable on them when profits are falling again.

(Student readers will find it useful to build up the Income Tax Account from the figures given above.)

In the above illustration, other sources of income and tax recoupable from annual payments are ignored. The first item would increase the debit for tax for the year the item was credited; tax recouped would reduce the tax to be charged for the year of recoupment.

In reserving, beneficial occupation of land and buildings must be included in the Schedule A tax. If in any year a Rule 21 assessment arises, the tax thereon must be reserved in full; this will involve no debit to Profit and Loss Account as the tax will have been recouped.

It must be borne in mind that the recommendations are an ideal at which all companies are advised to aim. Some may have found it difficult, but it is advised that, however gradual the process, steps in the right direction be taken as soon as possible.



The recommendations of the Institute of Chartered Accountants in England and Wales are set out below. These are prefaced with the remarks: "While it is recognized that the form in which accounts are submitted to shareholders is (subject to compliance with the Companies Act) a matter within the discretion of directors, it is hoped that these recommendations will be helpful to members in advising, in appropriate cases, as to what is regarded as the best practice."

*The treatment of taxation in accounts.*

The incidence of taxation and its effect on profits and on the financial position disclosed by the balance sheet, together with the extent to which the Inland Revenue on the one hand and shareholders on the other have participated in profits, are matters which should be made clear to shareholders.

The assessment of liability to National Defence Contribution and Excess Profits Tax is based on the profits of the accounting period under review. The assessment of liability to Income Tax is, however, for the fiscal year ending 5th April and is normally based on the profits of a preceding accounting period. The minimum or legal amount to be provided for taxation is thus the aggregate of taxes assessable on these bases, apportioned, as regards Income Tax, according to the period covered by the accounts under review.

Income Tax so apportioned takes no account, however, either of the balance of the liability assessable for the current fiscal year or of the liability which in normal circumstances will arise in respect of profits included in the accounts but not assessable until the following fiscal year. Further, unless provision be made year by year for Income Tax based on each year's results, the trend of net available profits will not be apparent, and cases will arise where the profits earned in a succeeding period will bear a disproportionate charge for taxation—indeed, they may even be insufficient to meet it.

In the case of principal and subsidiary companies (as defined in the Finance (No. 2) Act, 1939) Excess Profits Tax is assessable on the principal company in respect of the net excess profits of the group. The principal company has, however, the option of recovering from any subsidiary the tax charge relative to the excess profits of such subsidiary or of crediting any subsidiary with the tax benefit arising from the deficiencies of such subsidiary. The charge for taxation in the principal company's accounts thus depends upon the exercise (in whole or in part) of the option to allocate Excess Profits Tax over subsidiaries and may not be appropriate to the profits shown in the principal company's own accounts.

Recommendation.—It is therefore recommended that:—

(1) The charge for Income Tax should be stated in the accounts, and, subject to war-time or other special circumstances, the charge for National Defence Contribution or Excess Profits Tax should also be stated.

(2) (a) The charge for Income Tax should be based on the profits earned during the period covered by the accounts.

(b) Where it has been the practice to charge only the minimum or legal liability, then, until full provision has been made for Income Tax on all profits up to the date of the balance sheet, it is desirable—where possible—to make provision, in addition, for or towards the balance of the liability for the current and following fiscal years. This provision should be shown separately in the profit and loss account.

(c) Whatever method is adopted, the bases (i) of the charge and (ii) of any supplemental provision made for Income Tax should be disclosed.

(d) Income Tax on revenue taxed before receipt should be included as part of the taxation charge for the year and the relative income should be brought to credit gross.

(3) In the case of principal companies it should be indicated whether the provisions for Excess Profits Tax is in respect of the group or whether the sum charged has been arrived at after taking into account amounts allocated over subsidiary companies.

(4) Taxation charges may be affected by losses in the current period, deficiencies brought forward or adjustments of taxation in respect of previous periods, the effect of which, if material, should be disclosed. Any provision made in excess of the amount required to cover the estimated future liability on profits earned to date should, if material, be similarly disclosed.

(5) Any provision for (or in excess of) the estimated future liability to Income Tax in respect of the fiscal year commencing after the date of the balance sheet should not be included with current liabilities, but should be grouped with reserves or separately stated as a deferred liability and suitably described.

*The treatment in accounts of Income Tax deductible from dividends payable and annual charges.*

The payment of a dividend to shareholders does not affect the amount of tax payable by a company, the assessment being on the amount of the profits, as adjusted for the purposes of Income Tax. On the other hand, Income Tax deducted upon payment of debenture and other interest, royalties, and similar annual charges is in effect assessed on a company for collection from the payee.

Recommendation.—It is therefore recommended that :—

(1) (a) Whether dividends are described "less Income Tax" or "free of Income Tax" the amounts shown in respect thereof in the accounts should be the net amounts payable.

(b) Where a company continues the practice of providing for dividends gross the narrative should indicate that the distributions are subject to Income Tax. The taxation charge should be arrived at after taking credit for the tax deductible on payment of the proposed dividends.

(2) Annual charges for debenture and other interest, royalties and similar annual payments should be charged gross.

*The inclusion in accounts of proposed profit appropriations.*

Although certain appropriations of profits, including dividends recommended by directors, are subject to subsequent confirmation by shareholders, the inclusion of all appropriations in the accounts shows the amount which will be required for distribution to the shareholders and completes the accounts for the financial year by showing the results of trading and their application in one account. This course avoids the inclusion in the accounts of the next period of appropriations which are set out in the directors' report for the previous period, and have already been dealt with and disposed of. Also it facilitates the linking up of the accounts from one period to another, the balance carried forward to the following period being clearly shown in the accounts of each year.

Recommendation.—It is therefore recommended that :—

Provision be made in the books and in the annual accounts for proposed profit appropriations, those subject to confirmation by shareholders being so described. Provision for dividends should be shown as a separate item in the balance sheet.

By the Institute method, there will always be provided the tax due for the fiscal year in which the accounts end (if not already paid) and that for the next following fiscal year (usually estimated as to rate, since this will not always be known at the time the accounts are prepared). This is recommended as the only way to ensure that the amount which will be needed for tax on the actual profits is kept before the company, and retained available for when it has to be paid.

In the opinion of the editor, it is well to inset the gross amount of dividends and the tax deducted, so that shareholders can see the reason for the fluctuations in the net amounts.

By § 13 and 1st Schedule, Companies Act, 1947, when that Act comes into force, it will be obligatory in every Profit and Loss Account of a company, to show (a) the amount of the charge for United Kingdom Income Tax and other United Kingdom taxation on profits, including, where practicable, as United Kingdom Income Tax any taxation unpaid elsewhere to the extent of the relief, if any, from United Kingdom Income Tax and distinguishing, where practicable, between Income Tax and other taxation; (b) the basis on which the charge for United Kingdom Income Tax is computed; and (c) whether or not the amount stated for dividends paid and proposed is for dividends subject to deduction of Income Tax. ((b) and (c) may be by way of a note.) If there are arrears of fixed cumulative preference dividends, there must be a note or statement or report on the balance sheet showing the amount and period of the dividends in arrear (for each class when relevant), stating the gross amount unless the dividends are tax free, when the net amount

must be shown, but the fact that it is so shown must be stated. The basis on which the amount, if any, set aside for United Kingdom Income Tax is computed must also be shown by way of note on or in a statement or report annexed to the balance sheet.

### § 15.—Assessment of Share Profits.

A person who takes part in the promotion of a company or performs other services for it may receive payment in the form of shares issued as fully paid. It is then necessary to determine the amount of profit which he has made, which naturally depends upon the real value of the shares, which may be difficult to determine. It is usual in such a case, to agree with the Inspector of Taxes either (*a*) to have the shares valued, tax being paid on any excess of such value over the actual cost of obtaining the shares, or (*b*) for the assessment to stand over for a period of three years. Under method (*b*), if the shares are sold during the three years, any profit made must be reported to the Inspector of Taxes and tax paid thereon. At the end of the period the shares remaining unsold are valued at a price to be agreed according to any evidence that may be available, such as rates of dividend paid, market quotations, etc., and tax is then paid on the amount by which such valuation exceeds the original cost. In the event of failure to agree, the matter must be decided by the Commissioners (General or Special as selected).

It would seem, therefore, by analogy, that if profits of this nature are assessable in the first instance, and it is found on the final valuation that an actual loss has been sustained, such loss should be charged against profits under Schedule D, but it is more than probable

that the Commissioners would resist such a contention, on the grounds that such transactions do not fall within the description of a trade or profession (Cases I and II, Schedule D), but are within Case VI of Schedule D ; and the losses could therefore be utilised and carried forward only against Case VI assessments. (*See* Chap. VII, § 5.)

Where unrealised shares not already charged on their market value are distributed by way of dividend, their value, for the purpose of assessment on the company, is taken at the average selling price shown by the Stock Exchange lists for the month following the payment of the dividend. Where there is no market quotation, the value of the shares is determined by the Commissioners.

Where a company declares a dividend to be satisfied by the transfer of shares or stock in other companies held by the company as an investment (termed a "scrip dividend"), the amount thereof must be treated by the recipients as a "free of tax" dividend of an amount equal to the real value of the shares or stock so transferred (*Pool v. Guardian Investment Trust* (1922), 8 T.C. 167). Where the shares cannot be readily valued, the amount of the grossed dividend as declared must be included in the return, any adjustment being made when the shares are sold, or at the end of three years, similarly to the position explained above.

#### § 16.—Profits and Losses on Realisation of Investments.

Whether or not profits on the realisation of investments are assessable depends entirely on the facts of the case, and a decision of the Commissioners

(General or Special) will usually conclude the matter. If the person making the profit is shown to be dealing in investments, he is assessable under Case I of Schedule D, as a trader in investments and can claim relief for losses. If, on the other hand, it can be shown that the investments were held purely on capital account, any profit or loss on sale is a capital matter.

The distinction is well evidenced in the cases of a finance company and an investment company. The former is a dealer, and its investments stock-in-trade; the latter holds the investments solely as a means of earning income.

The fact that a company has power under its Memorandum of Association to purchase and sell investments is not conclusive evidence that it is trading in investments; the question to be determined is what actually constitutes its trading. The variation of investments may be merely incidental to, and not one of, its main objects.

Good examples will be found in *C.I.R. v. Scottish Automobile and General Insurance Co.* (1931), 16 T.C. 381, where the profits were held on the facts to be not assessable, and *Scottish Investment Trust Co. v. Forbes* (1893), 3 T.C. 231, where the profits were held to be assessable.

Occasional transactions resulting in the taking of profit on realisation of investments are not necessarily trading (*C.I.R. v. Scottish Automobile, etc., Co. (supra)*). If a company is formed for the purpose of dealing in securities, they are obviously assessable on profits made in so doing (*Californian Copper Syndicate v. Harris* (1904), 5 T.C. 160).

An exchange of securities on the Railways Amalgamation was held to be realisation in the case of *Royal Insurance Co. v. Stephen* (1928), 14 T.C. 22).

“Bond-washing” had reached considerable dimensions, and resulted in the loss of tax to the Revenue

prior to 1937-38. Briefly, the procedure was for the owner of securities to sell them to a dealer, *e.g.*, a finance company, at a price that included accrued dividend and buy them back, almost at once, *ex* dividend at a lower price. For example, a bearer security would be sold "*cum* interest;" the buyer would then cut off the coupon and sell the security back "*ex* interest." The difference in price would, of course, be less than the amount of the interest, so that the buyer would make a profit on the deal. The seller's profit, being of a capital nature, would not attract sur-tax. The buyer in such a transaction would often be a person not resident in this country, so that income tax as well as sur-tax was avoided.

For 1937-38 and subsequent years, these transactions are made abortive for the purpose of saving tax, as it is provided that in such a transaction the interest is to be treated as the income of the person who carried out the transaction, and the transaction is to be ignored in any dealer's accounts (§ 12—1937). "Security" includes stocks and shares.

These provisions apply not only where the collateral agreement is entered into directly between the owner of the securities and the person who takes in the securities, but also where it is entered into by either of them with someone else who may undertake the business. The provisions do not affect an ordinary *contango* transaction entered into on a stock exchange by a person who, having bought securities, does not take them up on the current account but carries them over, but it does apply to bond-washing transactions carried out in the form of *contango* contracts or by "borrowing the bonds."

Where the owner of any securities sells or transfers the right to receive the interest without parting with the securities, the income is to be deemed to be that of the beneficial owner of the securities (§ 24—1938).

§ 17.—(a) **Patent Expenditure** (§§ 35, 36—I.T.A. 1945).

Prior to 6th April, 1946, any expenditure in the outright purchase of patent rights, or for the future user for a period or over an area, and the cost of taking out new patents, was regarded as capital expenditure, not allowable as a deduction in computing profits, unless the trader concerned was a dealer in patents.

As from 6th April, 1946, a trader gets relief for capital expenditure on the acquisition of patent rights by outright purchase or licence, provided the patent rights or any rights out of which they were granted have not been sold or licensed for a capital sum before 6th April, 1946.

Royalties payable continue to be regarded as annual payments from which tax is deductible at source, renewal fees are allowable as revenue expenses as in the past.

Where the patents are used for the purposes of a trade, the trader is given relief by deduction from the assessment on the trading profits, *i.e.*, in the same way as wear and tear. If the allowances exceed the assessment, the balance goes forward, as in the case of wear and tear allowance, without time limit.

The capital expenditure on patent rights is allowed by equal annual instalments over—

- (a) 17 years ; or
- (b) if the remaining period of life of the patent is less than 17 years, over the remaining life ;  
or
- (c) if the period for which the rights are acquired is shorter than (b), that period.

The allowances begin in the year of assessment the assessment for which is based on the profits of the



accounting period in which the expenditure was incurred (*i.e.*, the rules as to basis periods are the same as for plant, etc.). (*See* § 3 of this Chapter.)

Should the trader sell the patent rights, or allow them to lapse, his annual allowances cease, but there will be a balancing allowance or charge to ensure that he has had during his ownership allowances equal to his net expenditure on them. The balancing allowance is the excess of the expenditure remaining unallowed over the proceeds of sale (if any). If the proceeds of sale exceed the unallowed cost, the excess will be the balancing charge which, however, is limited to the allowances already made; any further excess will be the subject of a separate charge. (*See* below.)

If there is a sale of part of the patent rights, *e.g.*, the grant of a licence for a given area, the proceeds of sale are deducted from the written down value of the patent rights, and future allowances calculated on the balance. Should the proceeds happen to exceed the written down value, there will be a balancing charge and no more annual allowances.

### Illustrations.

(1) Accounts made up to 31st December:—

Patent rights bought on 30th September, 1949, for £1,200  
—patent having 12 years to run—sold on 30th June, 1953.

	Case A	Case B	Case C
Cost .. .. .	£1,200	£1,200	£1,200
Annual allowance $\frac{1}{2}$ th of £1,200 = £100 from 1950- 51 to 1953-54—4 years	400	400	400
	<hr/> 800	<hr/> 800	<hr/> 800
Sale Price .. .. .	350	900	1,400
	<hr/> £450		
Balancing allowance 1954-55			
Balancing charge 1954-55		<u>£100</u>	<u>£400</u>
Balance assessable as ex- plained <i>post</i> (p. 286) ..			£200

(2) Accounts made up to 31st March. Patent rights bought 30th June, 1948, for £12,000 with 15 years to run. On 31st October, 1952, an exclusive licence is granted for certain territories for £5,500; and on 30th September, 1955, a further licence for £4,000.

Cost .. .. .	£12,000
Annual allowance ( $\frac{1}{15}$ of £12,000 = £800 per annum) 1949-50 to 1952-53 ..	3,200
Unallowed expenditure .. ..	8,800
Proceeds of partial sale .. ..	5,500
	<hr/>
	3,300
Future annual allowances (11 years to run, <i>i.e.</i> ) £300 per annum, for 1953-54 to 1955-56 .. .. .	900
Unallowed expenditure .. ..	2,400
Proceeds .. .. .	4,000
	<hr/>
Balancing charge .. .. .	£1,600

No more annual allowances will be given.

Had the second sale been for £7,000, there would have been a balancing charge on the allowances already given £3,200 + £900 = £4,700.

Proceeds £5,500 + £7,000 ..	= £12,500
Cost .. .. .	12,000
	<hr/>
Capital Profit .. .. .	£500

Assessable as explained *post* (p. 286).

A person other than a trader is entitled to allowances (a) if he is a resident in the United Kingdom, in respect of any patent right; (b) if he is not so resident, in respect of United Kingdom patent rights. The allowances are given by way of discharge or repayment of tax on patent income; any balance being carried forward, without time limit, to be set against future patent income. The allowances start on the year of assessment in which the expenditure is incurred.

Expenditure incurred on devising a patented invention is allowed in the year in which it is incurred

(as a deduction from the assessment as above). Fees for obtaining a patent, and similar expenses are deductible in the profits computation.

*(b) Receipts from sale of patent rights* (§ 37—I.T.A. 1945).

Receipts for the sale of patent rights that were capital before 6th April, 1946, are assessable if receivable on or after that date, provided the patent rights or any rights out of which they were granted were not sold or licensed before that date. Royalties, etc., from which tax is deductible, or receipts by a trader in patents—both already income receipts—are not affected (§ 64—I.T.A. 1945). Lump sums from the Crown for the acquisition of a defined portion of the property in a patent will be included (§ 43 (3)—I.T.A. 1945).

The charge covers any sale of patent rights by a resident in the United Kingdom, and the sale of United Kingdom patent rights by a non-resident. A resident is entitled to deduct the cost of acquisition by him, and is assessable under Case VI of Sch. D over six years beginning with the year of receipt, unless he elects within 12 months from the end of the year of assessment, to be charged on it all in the year of receipt.

If the seller dies before the beginning of the sixth year of assessment, the unassessed balance will be treated as income of the year of death. Similar treatment applies on the winding-up of a company (the commencement of the winding-up being the appropriate date) or dissolution of a partnership. In the latter case, the income is apportionable over those who were partners immediately before the discontinuance, and each partner is assessed separately.

The personal representatives of a deceased seller, and each partner in a dissolved partnership, have the option, however, of claiming that the extra tax payable for the year of death (or dissolution), shall be reduced to the tax that would have been payable had the unassessed balance been taxed by equal instalments in each of the years to that date. The claim must be made within 21 days after the service of the notice of assessment on the unassessed balance.

Where a non-resident sells rights under a United Kingdom patent for a capital sum, the purchaser must deduct tax from the price at the standard rate of the year of payment, and pay it to the Revenue. The non-resident can reclaim tax on the cost to him of acquiring the rights and on the basis of spreading the capital sum over six years. The claim must be made within 12 months from the end of the year of assessment.

(c) *Miscellaneous.*

Relief for expenses incurred in the actual devising of a patented invention is given (unless already allowed under some other provision, *e.g.*, research expenditure) (§ 39—I.T.A. 1945). If incurred after 5th April, 1946, the expenses are allowable in full in the year on which the expenditure was incurred; if incurred earlier, there must be deducted from the expenses as many seventeenths as there were complete years between the date of the patent and 6th April, 1946, the balance being allowable in 1946-47. A trader gets the allowance as a deduction in the assessment; any one else by set-off against patent income; any balances being carried forward.

Patent Office fees, agents charges, etc., paid after 5th April, 1946, in obtaining a patent or extension of

a patent for use in a trade, are deductible in the accounts. A non-trader gets relief by deduction from patent income as above.

*(d) Royalty payments.*

Where a patentee for 1945-46 or later receives royalties or other payments for use of a patent, and the payment covers a period of six years or more, he can claim to have his liability to Income Tax (and Sur-tax) adjusted to what it would have been had the income been spread equally over the six years up to and including the year of receipt. If the period is less than six years but not less than two, the spread is over the number of complete years of user (§ 41—I.T.A. 1945.) (This includes chargeable capital sums (§ 43 (1)—I.T.A. 1945).)

Patent income from a patentor's own inventions is earned income for 1946-47 onwards. If someone else is interested, the claimant gets the earned relief on that part of the income which corresponds to the share in the patent which never belonged to anyone else (§ 40—I.T.A. 1945).

*(e) Anti-avoidance provisions.*

If the sale is between persons in common control, or the main object of the transaction appears to be obtaining allowances, the market value of the rights sold is substituted for the actual price, and allowances given to all parties accordingly. Where, however, the case is one of common control only, the parties may decide to substitute the "unallowed expenditure," i.e., written down value if that is less than the market value (§ 59—I.T.A. 1945).

### § 18.—Trade Marks and Designs.

There are allowed as expenses chargeable in the accounts any fees paid or expenses incurred on or after 6th April, 1946, in obtaining for the purposes of a trade, the registration of a design or of a trade mark or the extension of the period of copyright in a design or renewal of registration of a trade mark (§ 62—*I.T.A.* 1945).

### § 19.—Mines, Oil Wells, etc.

The Income Tax Act, 1945, Part III, gives relief for the expenditure incurred in connection with the working of a mine, oil well or other source of mineral deposits of a wasting nature—

- (a) a searching for, or on discovering and testing deposits, or winning access thereto ; or
- (b) on the construction of any works which are likely to be of little or no value when the source is no longer worked, or where the source is worked under a foreign concession, which are likely to become valueless when the concession comes to an end to the person working the source immediately before the concession comes to an end.

The following expenditure is not included :—

- (i) acquisition of the site of the source or the site of any such works, or of rights in or over any such site ;
- (ii) acquisition of, or of rights in or over the deposits ;
- (iii) plant or machinery (this attracts wear and tear, etc.) ;
- (iv) works constructed for subjecting the raw product to any process other than preparing it for use as raw product ;

- (v) buildings or structures provided for occupation by or for the welfare of workers (these will attract allowances under the "industrial buildings" provisions—*see* § 4 of this Chapter—(§ 8 (3)—I.T.A. 1945)).
- (vi) buildings constructed wholly as offices ;
- (vii) so much of a building as is constructed for use as offices, unless the part so used does not exceed 10 per cent. of the whole.

The allowances, which are an initial allowance and annual allowances, are given in the same way as wear and tear allowances. The initial allowance is 10 per cent. of the capital expenditure on (b) above made on or after 6th April, 1946 ; and of 10 per cent. of the expenditure on (a) or (b) above on or after 6th April, 1944, and before 6th April, 1946, less any mills, etc., and exceptional depreciation allowances made before 6th April, 1946. No initial allowance is made if the asset has been sold before 6th April, 1946.

The annual allowance is calculated by reference to the output during the basis period. The fraction of the residue of the expenditure to be allowed in any year of assessment is found by taking as numerator the output of the basis period, and as denominator the sum of that output and the total potential for some output of the source estimated at the end of the basis period. The fraction for any year of assessment, however, is not to be less than one-twentieth.

The "residue of the expenditure" means the original expenditure less—

- (i) the initial allowance for that or any previous year ;

- (ii) any annual allowances already made ;
- (iii) any exceptional depreciation allowances made up to 5th April, 1946 ;
- (iv) (a) any sale, insurance, salvage or compensation moneys ; but  
(b) if the business is sold as a going concern, there is to be deducted, not the sale price, but the residue of expenditure.

Should the source cease to be worked, or the concession end, the claimant may elect to have the annual allowances for the year of assessment in which the event occurs and the previous five years, recomputed as if the denominator of the fraction were the actual output of the basis period plus the output between the end of the basis period and the cessation.

If the business in question was being carried on on 6th April, 1946, allowances as if there had been incurred on that date an amount of expenditure ascertained as follows :—

- (1) From the total eligible expenditure incurred before 6th April, 1946, deduct—
  - (a) any expenditure attributable to any asset already sold ;
  - (b) any mills, etc., or exceptional depreciation allowances made to that date on assets not already sold.

(2) Ascertain the fraction whose numerator is the total potential output at 6th April, 1946, and whose denominator is the total output to that date added to such potential output.

(3) Apply (2) to (1) and the result is the required amount.



If the trader considers this to be inadequate, having regard to the dates on which expenditure was incurred, he can apply to the General or Special Commissioners, who may authorise an increase.

Should the person carrying on the trade have purchased from a predecessor assets representing expenditure that is covered by this Part of the Act, the amount of the expenditure on which he gets allowances is the smaller of—

- (A) An amount calculated as in (1)—(3) above (including the predecessor's expenditure), but deducting in (1) any assets sold by the predecessor as well as by the trader.
- (B) (1) add to the price paid by the trader, all eligible expenditure incurred by him before 6th April, 1946, and deduct—
  - (a) expenditure attributable to assets sold ;
  - (b) the price paid for assets acquired from the predecessor and sold by the trader before that date ;
  - (c) any relevant mills, etc., or exceptional depreciation allowances up to 6th April, 1946.
- (2) Apply the fraction whose numerator is the total potential future output, and whose denominator is the sum of the future output and the actual output since the date of acquisition.

Where a source or part of a source is sold as a going concern, a balancing allowance or balancing charge will be made in respect of the difference between the residue of expenditure and the proceeds. The allowance or charge will be adjusted, however, where the source was working when the 6th April, 1946, arrived, by applying the fraction : total output from 6th April,

1946, to date of sale, over total output from the beginning to the date of sale. The balancing allowance in such a case is subject to appeal to the General or Special Commissioners, who may allow a smaller reduction if they think it excessive having regard to the dates of expenditure.

The balancing charge is not to exceed the excess of the expenditure incurred by the vendor over the residue of expenditure.

The buyer will get annual allowances and balancing allowances or charges, by reference to the lower of—

- (a) the price attributable to the assets ;
- (b) the residue of expenditure immediately after the sale.

Expenditure prior to starting business is deemed to be incurred on the day the business starts, but no initial allowance will be given on expenditure before 6th April, 1944.

A person who incurs expenditure in searching for, discovering and testing mineral deposits and having access to them, and sells the assets before trading, will get no allowances, but the buyer will get allowances on the expenditure in question on the price paid by him, whichever is smaller.

The Commissioners of Inland Revenue are to make Regulations for determining the extent of mineral deposits and the basis on which potential output is to be estimated, etc.

#### Illustration.

An established mine incurred expenditure in the year to 31st December, 1947, (a) on testing and winning access to deposits £1,000, (b) on constructing works which will be useless when the deposit is exhausted £8,000.

In the following year the expenditure was (a) £400, (b) £3,000.  
The output was as follows :—

	1947 tons	1948 tons	
Actual output of year ..	10,000	15,000	
Potential output at end of year	230,000	210,000	
Allowances :—			
1948-49			
Initial allowance 10% of £8,000		£800	
Annual allowance :—			
10,000			
————— × £(1,000 + 8,000 - 800)			
10,000 + 230,000			
But $\frac{1}{10}$ th is greater .. ..		410	
		—————	1,210
1949-50 Initial allowance 10% of £3,000		£300	
Annual Allowances :—			
Expenditure in 1947 .. ..	£9,000		
Less allowed .. ..	1,210		
	—————		
	7,790		
Expenditure in 1948 .. £3,400			
Less Initial allowance .. . 300			
	—————		
	3,100		
	—————		
	£10,890		
	—————		
15,000			
————— × £10,890		726	
15,000 + 210,000		—————	1,026

Note.—It will be observed that whilst the annual allowance is granted on the expenditure incurred under both (a) and (b), the initial allowance is given only on the cost of constructing works which will be of little or no value when the source is no longer worked.

## CHAPTER V.

## SCHEDULE D.

## CASES III, IV AND V.

## § 1.—Income of Uncertain Annual Value.

Under Case III of Schedule D are assessed—

Income from  $3\frac{1}{2}\%$  War Stock (except (a) Bearer Bonds, which are taxed at source, and (b) where the taxpayer has required tax to be deducted at source);

The discount on Treasury Bills,

Bank and other short loan interest from which tax is not deductible at source, not being "yearly interest";

Dividends from public revenue not exceeding £2 10s. 0d. per half-year (since tax is not deducted at source therefrom);

Tithes, fines for renewal of leases, etc.;

Profits on all securities bearing interest payable out of the public revenue (where not charged under Schedule C, e.g., Government Stocks bought through the Post Office);

Interest and dividends received from co-operative and similar societies;

Interest on War Damage Contributions paid in advance (§ 62 (5) War Damage Act, 1943);

All other interest which is not annual interest.

Sums received under insurance policies during sickness or disablement can be assessed (*Forsyth v. Thompson*, (1940), T.R. 387).

The practice appears to be to regard as assessable benefits which continue for a period exceeding 12 months, but only from the expiration of such 12 months.

Small maintenance payments from which tax is not deductible as a result of § 25—1944. Tax is computed on the payments falling due in the year of assessment, so far as paid in that or in any other year (§ 25—1944).

Interest on tax reserve certificates is exempted from tax.

If the Commissioners find that lands charged under Sch. B on the assessable value, and which are occupied by a dealer in cattle or a dealer in or seller of milk, are insufficient for the keep of the cattle brought on the lands SO THAT THE ASSESSABLE VALUE AFFORDS NO JUST ESTIMATE OF THE PROFITS, they may charge under Case III the excess of the profits over the Sch. B assessment. "Cattle" includes pigs and horses (*Phillips v. Bourne* (1947), T.R. 25). The Acts do not provide for Wear and Tear or Obsolescence Allowances, or the carrying forward of losses in such cases.

The basis of assessment under Case III is the income arising in the preceding year of assessment, no account being taken of accruing income. The rules for new sources may be summarised thus—

<i>Year of Assessment.</i>	<i>Assessment.</i>
Year in which the income first arises.	Actual income from date when income first arises to 5th April following.
Second year.	Actual income of second year unless the income first arose on 6th April in the first year when assessment is on previous year's income.
Third year.	Previous year's income.

The first assessment which is based on the preceding year's income (this is normally the assessment for the third year, but if the first year was a full year, then it is that of the second year) can be reduced to the actual income of the year of assessment, on a claim being made to the Inspector of Taxes within twelve months after the end of the year of assessment.

In other words, the assessment is on the actual income until there is a full preceding year, when the previous year's income is the basis of assessment;

the first assessment based on the previous year's income can be reduced to the actual income of the year of assessment.

### Illustration.

Date when income first arose.	Year of Assessment.	Basis of Assessment. Actual Income received during.
6th April, 1945.	1945-46.	Year ended 5th April, 1946.
	1946-47.	Year ended 5th April, 1946, or
		Year ended 5th April, 1947, if
		claimed by taxpayer.
		Year ended 5th April, 1947.
After 6th April, 1945 and before 6th April, 1946.	1947-48.	
	1945-46.	Year ended 5th April, 1946.
	1946-47.	Year ended 5th April, 1947.
	1947-48.	Year ended 5th April, 1947, or
		Year ended 5th April, 1948, if
		claimed by taxpayer
	1948-49.	Year ended 5th April, 1948.

In all subsequent years the basis of assessment is the actual income received during the preceding year (§ 17—1922). So long as the source continues, Income Tax is chargeable on the basis of the income of the preceding year even if no income arises from the source in the year of assessment (§ 22—1926). Where a person ceases to hold a source, the assessment for the ultimate year is on the actual income, and the Revenue have the power to increase the assessment of the penultimate year to the actual income (§ 30—1926).

Additions to a source are assessed as separate sources according to the rules for new sources, until the preceding year basis operates, when the source is treated as one. Similarly, where part of a source is sold or otherwise parted with, the income on that part is assessed according to the discontinuance rule, only the income on the remainder of the source continuing to be assessed on the preceding year basis (§ 30—1926).

## Illustrations.

(1) A had £30,000 on deposit at his bankers. On 31st March, 1947, he withdrew £12,000. The interest received was as follows :—

Year ended 31st March, 1945,	£300.
“ “ “ “ 1946,	£320.
“ “ “ “ 1947,	£280.

The assessments would be as follows :—

Year.	Original Assessments.	Amended to : On £18,000 left on deposit.	On £12,000 withdrawn.	Total.
1945-46	£300 $\frac{18}{30} \times$	£300 = £180	$\frac{12}{30} \times$ £320 = £128 (being penultimate year.)	£308
1946-47	£320 $\frac{18}{30} \times$	£320 = £192	$\frac{12}{30} \times$ £280 = £112	304
1947-48	£280 $\frac{18}{30} \times$	£280 = £168	—	168

Thereafter, the assessments will be upon the income arising in the preceding year, since only the £18,000 is then involved.

(2) B had £30,000 on deposit at his bankers. On 1st January, 1946, he deposited a further £18,000. The interest credited to his Current Account was as follows :—

Year ended	31st December, 1944	.. ..	£299
Half-year ended	30th June, 1945	.. ..	140
“	31st December, 1945	.. ..	160
“	30th June, 1946	on £30,000	150
		on £18,000	90
“	31st December, 1946	on £30,000	155
		on £18,000	93

Year.	Assessments on £30,000	On £18,000
1945-46	Preceding Year = £299	Nil, no income having been received.
1946-47	do. £300	Actual income of year = £183.
1947-48	do. £305	Preceding year = £183. This may be reduced to “actual” if less than £183.

Thereafter, the income from the £48,000 will be assessed on the “preceding year” basis. For purposes of Income Tax, deposit interest is taken to arise when it is actually credited to the account of the depositor.

Where a security, carrying interest which is payable without deduction of tax, is sold *cum* dividend between two dividend dates, the portion of the purchase price representing the accrued interest to the date of sale is not assessable to Income Tax in the hands of the vendors (*Wigmore v. Summerson & Sons* (1925), 9 T.C. 577). The recipient is assessed in respect of the full dividend or interest in such cases.

The proportion representing interest, accrued since death, included in instalments on a moneylender's promissory notes received after his death, is assessable under Case III on his legal personal representative (*Bennett v. Ogston* (1930), 15 T.C. 374), as it is interest for the use by the borrower of the money which remains unpaid.

Where Victory Bonds are transferred to the Commissioners of Inland Revenue in payment of estate duty, the accrued interest forming part of the value at which the Bonds are accepted is not assessable to Income Tax (*Monks v. Fox's Executors* (1928), 13 T.C. 171).

## § 2.—Foreign and Dominion Profits.

### (a) Domicil of Taxpayer.

By domicil is meant the place of abode of an individual to which, when absent, he intends to return; the country upon which he looks as his natural home. It may be a domicil of origin or choice.

The domicil of origin is not the actual place of birth, but that arising from a man's birth and connections. Thus the domicil of origin of a son of an English father follows that of the father, even though the child be born abroad.



The domicile of origin cannot be lost by being merely abandoned, but remains the domicile of the individual until a new one is acquired; and therefore in order to substitute a domicile of choice he must acquire such new domicile, and abandon his domicile of origin or previous domicile of choice, after manifesting his intention to do so (*Somerville v. Somerville*, 5 Ves. 750; *Bonneval v. De Bonneval*, 1 Curt. 864).

If, however, the domicile of choice is abandoned, the domicile of origin revives (*King v. Foxwell*, 3 C.D. 518).

A domicile may also be acquired by operation of law, *e.g.*, on marriage.

*Primâ facie* the place of residence is the domicile, but this may be rebutted. A man may have different residences in different countries, and yet he will have only one legal domicile (*Cooper v. Cadwalader*, (1904), 5 T.C. 101).

Thus, a man may be resident in this country and carrying on business here, without having abandoned his foreign domicile or his ultimate intention to return thereto; and, while he is subject to taxation in the ordinary way on the profits derived from his English business, he nevertheless may gain a decided advantage in connection with his foreign profits.

A company has a domicile in the country in which it is registered, and cannot change it (*MacNaghten, J.*, in *Gasque v. C.I.R.* (1940), T.R. 255).

#### **(b) Residence of Taxpayer.**

Residence is a matter of physical presence as well as intention, and is a question of fact, to be decided upon by the Commissioners. Domicil and residence are matters on which an appeal can be made to the Special Commissioners from a decision of the Commissioners of Inland Revenue (§ 27—1924).

A person can have but one domicile, but he may be "resident" in several countries at the same time.

The Board of Inland Revenue have prepared the following statement for the assistance of visitors to the United Kingdom :—

"A visitor who maintains no place of abode in the United Kingdom and whose visits are not habitual, but occasional only, is not regarded as resident in the United Kingdom, unless he has been in the United Kingdom for a period or periods equal in the whole to six months in the Income Tax year (beginning 6th April).

"If, however, he maintains a place of abode in the United Kingdom, available for his use, he is regarded as resident for any year in which he pays a visit, of whatever length, to the United Kingdom.

"Moreover, though he does not maintain a place of abode in the United Kingdom available for his use, and does not stay for six months in any one year, he is regarded as becoming resident if he visits the United Kingdom year after year (so that his visits become in effect part of his habit of life), and the annual visits are for a substantial period or periods of time. The question of residence in any particular case can only be determined by reference to the facts of the case. But it can be said that the Board of Inland Revenue would normally regard an average annual period or periods amounting to three months as 'substantial,' and the visits as having become 'habitual' after four years. And, where the visitor's arrangements indicated from the start that regular visits for substantial periods were to be made, he would be regarded as resident in and from the first year."

Residence does not imply keeping up an establishment; the physical fact of being in the country, *e.g.*, living in hotels, etc., is just as much residence.

A person is not chargeable to tax under Schedule D as resident in the United Kingdom, in respect of profits from possessions or securities outside it so long as—

- (a) he IS IN THE UNITED KINGDOM FOR SOME TEMPORARY PURPOSE ONLY, and not with a view or intent of establishing his residence therein, AND
- (b) he HAS NOT actually RESIDED in the United Kingdom at one time or several times *for a period equal in the whole to six months in the year of assessment.*

If, however, any such person resides in the United Kingdom for at least six months in the Income Tax year he is chargeable for that year (Sch. D, Misc. Rules, R.2).

The rules are applied generously in the case of persons whose change of residence has been forced on them by the war (*see* Appendix XV).

Persons not resident in the United Kingdom are liable to assessment in so far as they derive income from real or personal estate, trade or employment in the United Kingdom (General Rules) and can claim no allowances or deductions (§ 24—1920), except in the cases dealt with in Chapter II, § 23.

The question of each year's liability must be looked at as a separate issue, but the facts over a period of years can be looked at so as to get the "one continuous story" as bearing on the year in question (*Levene v. C.I.R.* (1928), 13 T.C. 486 (*see* Viscount Sumner's judgment)).

A person maintaining an establishment here is deemed to be resident here in any year in which he visits this country, no matter for how short a period. Where a person has been resident in the United Kingdom in the past, it is very difficult for him to prove non-residence in any subsequent year, unless he is actually out of the country for the whole year and can prove that it is not his intention to return.

A person ordinarily resident in the United Kingdom is assessable to Income Tax, even though temporarily absent for some portion of any year, but if he has retained a foreign domicil, his liability in respect of foreign income will be qualified by that fact.

In practice, a seafaring employee is treated as employed wholly in the United Kingdom if his ship sails exclusively between ports in the United Kingdom, and as employed wholly abroad if his ship sails exclusively between ports outside the United Kingdom. If his ship sails between ports in the United Kingdom and ports abroad, he is treated as exercising his employment partly in this country and partly abroad.

A seafaring man, absent for the whole year, is still "resident" if he maintains a residence or (apparently) a wife and family here (*Rogers v. Inland Revenue* (1879), 1 T.C. 225). But if he receives and banks his salary abroad, he will be assessed only on remittances under Case V, and not under Schedule E, as would be the case if he received his salary in the United Kingdom. Seafaring cases, however, are founded on very old cases, and are not of general application.

When a person formerly not resident is held to become resident in any year he is regarded as resident for the whole year of assessment, though income formerly not assessable in the United Kingdom is usually only assessed as from the date of his becoming resident.

**(c) "Resident" and "Ordinarily Resident."**

For some purposes, the Acts draw a distinction between a person who is "resident" and a person

who is "ordinarily resident" in the United Kingdom. The distinction is very finely drawn, but it can be said that a person may become technically resident without becoming ordinarily resident.

Possibly the term "ordinarily" is best regarded as the converse of "occasionally." A person may become technically "resident" in a year, *e.g.*, if he is here for a temporary purpose and stays for over six months in the fiscal year, but could not be said to be "ordinarily resident." If his visits are regular, however, it becomes part of his ordinary habit of life to live a substantial portion of each year here, and he is thus "ordinarily resident."

"I think that [ordinary residence] connotes residence in a place with some degree of continuity and apart from accidental or temporary absences" (*Levene v. C.I.R.* (1928), 13 T.C. 486 *per* Lord Cave).

"If it ('Ordinarily resident') has any definite meaning I should say it means according to the way in which a man's life is usually ordered" (*Levene v. C.I.R.*, *supra*, *per* Lord Warrington of Clyffe).

" . . . . . the word 'resident' indicates a quality of the person charged and is not descriptive of his property, real or personal. To ask where he has his residence is often a convenient form of inquiry but only as leading to the question: 'Then where is he resident himself?' " (*Lysaght v. C.I.R.* (1928), 13 T.C. 511, *per* Viscount Sumner).

" . . . . . if the periods for which and the conditions under which he stays are such that they may be regarded as constituting residence, it is open to the Commissioners to find that in fact he does so reside, and, if residence be once established, 'ordinary

residence' means in my opinion no more than that the residence is not casual and uncertain but that the person held to reside does so in the ordinary course of his life" (*ibid. per* Lord Buckmaster).

**(d) Case IV—Dominion and Foreign Securities.**

Under Case IV of Sch. D is assessed the income arising from securities out of the United Kingdom except such income as is assessed under Sch. C. "A security is a possession such that the grantee or holder of the security holds as against the grantor a right to resort to some property or some fund for the satisfaction of some demand, after whose satisfaction the balance of the property or fund belongs to the grantor. There are two owners, and the right of the one has precedence over the right of the other. A share in a corporation does not answer the above description" (*Singer v. Williams* (1921), 1 A.C. 41, *per* Lord Wrenbury). To come under Case IV, therefore, the securities must be of the nature of mortgages or bonds, or Foreign or Dominion Government or Public Authority Stocks not assessed under Sch. C.

The basis of assessment is the same as under Case III, *i.e.*, on the income arising in the year preceding the year of assessment. It is immaterial whether the income has been or will be received in the United Kingdom or not. If the income is left abroad and not received in the United Kingdom, the same deductions and allowances apply as if it had been so received. In assessing income under Case IV, deductions are allowed for Income Tax paid in the place where the income has arisen (subject to the qualification dealt with under Dominion Income Tax Relief in Chapter X), and for annual interest or any annuity or other annual

payment payable out of the income to any person not resident in the United Kingdom. Foreign Income Tax levied on profits which are not assessable to Income Tax in this country cannot, however, be deducted from income which is assessable here (*Scottish American Investment Co. v. C.I.R.* (1938), S.C. 234).

The basis of assessment is modified in the case of—

- (a) any person who satisfies the Commissioners of Inland Revenue that he is not domiciled in the United Kingdom, or that, being a British subject, he is not ordinarily resident in the United Kingdom ; or
- (b) income arising from foreign or dominion securities which form part of the investments of the Foreign Life Assurance Fund of an Assurance Company.

In such cases, the assessment is on the amounts remitted to this country in the preceding year out of income. (*See* also Chap. X, § 16, as to securities in Eire.)

As regards new and discontinued sources, the rules of assessment are the same as for Case III, including those applicable to increases and decreases in holdings.

**(e) Case V—Dominion and Foreign Possessions.**

Under Case V of Sch. D is assessed the income arising from possessions out of the United Kingdom. Except in the case of income which—

- (a) is immediately derived by a person from the carrying on by him of any trade, profession or vocation either solely or in partnership, or

(b) arises from any office, employment or pension, the basis of assessment is the same as under Case IV, *i.e.*, on the income arising in the preceding year, subject to the same deductions. In the case of rent, a deduction is allowed for the cost of repairs, management and insurance of the property from which the rent is derived.

Income from possessions mentioned in (a) and (b) above, *i.e.*, earned income, is assessed on the basis of the amount remitted to this country in the preceding year (§ 19—1940).

Under Case V, like Case IV, the remittance basis also applies to a person who is not domiciled in the United Kingdom, or who, being a British subject, is not ordinarily resident therein, and to the income arising from the investments of the Foreign Life Assurance Fund of an Assurance Company. (*See also* Chap. X, § 16, as to possessions in Eire.)

In the case of the remittance basis, it is not possible to avoid liability by means of what are usually termed "constructive remittances," *e.g.*, stocks purchased abroad out of earned income and brought to this country, set-off, income imported in kind, will all count as remittances.

Where income from foreign possessions assessable on a remittances basis is paid into a bank abroad, and advances are made here by the English branch of the same bank, neither the loans nor the transfer of the loans to the bank abroad can be treated as remittances of income to this country. The loans went to meet the money, not the money to meet the loans (*Hall v. Marians* (No. 2) 1936, 19 T.C. 582).

If separate banking accounts are kept for income and capital, remittances out of the latter account cannot be considered to be



constructive remittances of income, when they are in fact of capital (*Kneen v. Martin* (1934), 13 A.T.C. 454).

The Rules governing assessment in the early years of possession of a source of income assessable under Case V, and the discontinuance of, additions to, and the sale of part of, a source under those cases, are the same as those already enumerated for Case III. (See Chap. V, § 1.)

All profits or income in respect of which a person is chargeable under Case III (excluding the investment income of Dominion and Foreign Life Assurance Companies, and the profits of cattle dealers and milk sellers), Case IV or Case V may be assessed and charged in one sum (§ 30—1926).

Where any income previously assessable under Case IV or Case V becomes chargeable by deduction at source, the source is treated as discontinued, and the provisions governing discontinued sources apply accordingly. Similarly, where income previously charged by deduction at source becomes liable under Case IV or V, it is treated as a new source (§ 30—1926).

When a business formerly assessed under Case V as a foreign possession becomes liable under Case I owing to change in the place of control, it is not to be assessed as a new business (*Fry v. Burma Corporation* (1930), 15 T.C. 113), but as a continuing business. When a business formerly assessed under Case I shifts control and becomes assessable under Case V, it would appear that the Case V assessment of the first year should be based on the income of the previous year, but assessments raised under Case V cannot include any dividends distributed while the company was controlled in the United Kingdom (*Bradbury v. English Sewing Cotton Co., Ltd.* (1923), A.C. 744).

The same principle extends to the income of an individual who comes to this country after residing

abroad. If such an individual had a source of income outside this country before coming here, this source is not treated as a new one for purposes of Income Tax. Income must be regarded as first arising when it first arose as an income and not when the possessor of it "swam into the purview of the Income Tax Acts." If a person who becomes resident has held a source for some years, the preceding year basis and not the new source rules will therefore apply (*Back v. Whitlock* (1932), 16 T.C. 723).

A person assessable on remittances is charged on the footing that the income first arose on the date it was first received in the United Kingdom after he became resident. He is not charged for the first year of residence on more than the income arising abroad from the date he took up residence to the end of the year of assessment. If the foreign sources ceased prior to his becoming resident, no assessment can be raised on money brought to this country after such cessation.

Under the heading of possessions will come every source of income, except such as the Legislature has specifically termed securities. It includes, therefore, the interest which a person resident in this country possesses in a business carried on and controlled entirely abroad by a foreign firm (*Colquhoun v. Brooks* (1889), 59 L.T. 850). An assessment under Case V in respect of salary and commission payable in this country under a contract of employment as agent abroad for a British company, where the agent was resident in the United Kingdom, has been held to be bad, since the salary being paid in this country, no remittance was possible (*Pickles v. Foulsham* (1925), A.C. 458); the assessment was therefore under Schedule E and not Case V of Schedule D. But in

similar circumstances, where the salary was *payable* abroad, the agent was held to be liable under Case V on sums remitted to this country (*Fleming v. Wilkinson* (1925), 10 T.C. 416). A non-resident director of an English company is assessable under Sch. E on his fees (*McMillan v. Guest* (1942), T.R. 79).

Assessment under Case V on income from employments is not confined to those wholly carried on outside the United Kingdom; the test for ascertaining the source of income is not the place where the activities of the employee are exercised, but the place where the income really comes to the employee. Where a substantial part of the duties of the employee, resident in England, under a contract of employment made abroad with a foreign company, was performed in the United Kingdom, but by arrangement the salary was paid into a banking account abroad, it was held that the employee was assessable under Case V on a remittances basis (*Bennet v. Marshall* (1938), 1 K.B. 591). But where the remuneration is payable in the United Kingdom to a resident, Sch. E applies (*McKenna v. Eaton-Turner* (1936), 20 T.C. 566) (*see below*).

The Report of the Income Tax Codification Committee states (§ 82) that they were informed that the practice of the Board of Inland Revenue with regard to employments other than public employments, based on their interpretation of Rule 1 (a) (ii) and (iii) of Schedule D, and the decision in *Pickles v. Foulsham* ((1925), A.C. 458; 9 T.C. 261) is as follows:—

“ A.—*Residents.*

- (i) Where the duties are wholly or partly performed in the United Kingdom, the full emoluments are charged under Schedule E;

- (ii) Where the duties are wholly performed abroad—

(a) the full emoluments, if the emoluments are normally received, wholly or in part, in the United Kingdom, are charged under Schedule E ;

(b) the emoluments, if wholly received abroad, are, so far as they are remitted to the United Kingdom, charged under Case V of Schedule D.

An exceptional receipt of emoluments in the United Kingdom, *e.g.*, when the employee is on leave here, is not treated as involving liability under Schedule E."

" B.—*Non-residents.*

- (i) Where the duties are wholly or partly performed in the United Kingdom, the emoluments, to the extent to which the duties are performed in the United Kingdom, are charged under Schedule E.
- (ii) Where the duties are wholly performed abroad, there is no liability" (*but see McMillan v. Guest (supra)*).

A person resident in England (having a house here in which his family lived), employed in West Africa, by an English company controlling their business from England, performing all his duties in West Africa, but the greater part of whose remuneration was paid by the company into his bank in England, was held to be assessable under Schedule E (*McKenna v. Eaton-Turner* (1937), A.C. 162). This decision agrees with the practice of the Revenue as set out in A (ii) (a) above.

In the case of employments exercised wholly abroad, where the remuneration is payable abroad, the assessment will be on remittances under Case V. Crown officials paid out of the public revenue of this country are assessable under Schedule E, but an officer who serves at a foreign station and does not maintain a residence in the United Kingdom may claim to be a non-resident in any year in which his foreign service includes a complete fiscal year. In such a case as the latter, a wife resident here may be assessed as a *feme sole*, but her husband's remittances out of his foreign salary or profits are not assessable upon her unless received by her under contractual obligation. But alimony received by a British woman from a foreign divorced husband has been held to be a receipt from a "foreign possession" (*C.I.R. v. Anderström* (1927), 13 T.C. 482).

The exemption from tax of the interest on  $3\frac{1}{2}\%$  War Loan, and certain other stocks in the beneficial ownership of a person not ordinarily resident in the United Kingdom, is given if the securities belong to a married woman not ordinarily resident. The ordinary residence of her husband is not material, except in so far as it may afford assistance in determining that of the wife (Report I.T.C.C.).

If, however, the husband is not resident, but the wife is resident, if she is still technically "living with her husband" he is the proper person to be assessed and no assessment on  $3\frac{1}{2}\%$  War Loan interest can be made upon him (*Browning v. Duckworth* (1935), 19 T.C. 149). If, however, the husband visits this country, the assessment in respect of the wife's income can be made on him on such a visit although he is not resident (*Duckworth v. Lowe* (1937), 2 K.B. 560).

Where any trade or business is carried on by two or more persons in partnership, and the control and management of the business are situate abroad, the

business is deemed to be carried on by persons resident outside the United Kingdom. The partnership is deemed to reside outside the United Kingdom, notwithstanding the fact that some of the members of the firm are resident in the United Kingdom, and some of the trading operations of the firm are conducted in the United Kingdom (Rule 12, Schedule D, Cases I and II).

In such cases the firm is assessable in respect of the trading operations conducted in the United Kingdom only to the same extent as a person resident abroad is assessable in respect of trading operations by him within the United Kingdom, and the assessment may be made in the name of any resident partner (*ibid.*).

In order that advantage can be taken of these provisions it is essential that the foreign operations be under the control of the foreign partners and that the partnership deed substantiates this fact; the foreign profits will then be assessable under Case V. If, however, all the partners reside in the United Kingdom, the control will clearly rest in the United Kingdom, and profits of the whole business will be assessable under Case I; but the practice is to exclude from the assessment the share of a non-resident partner in respect of profits earned abroad.

Where a foreign firm buys goods and a British firm sells them on joint account, the whole profits of the joint account are assessable as a partnership (*Morden Rigg & Eskrigge v. Monks* (1923), 8 T.C. 450).

**(f) Case I or Case V, Schedule D.**

Income arising to a person resident in the United Kingdom from any trade or business outside it will be

charged to tax under either Case I or Case V, whichever is appropriate.

If the business is effectively controlled from the United Kingdom, then the profits will be assessed under Case I, Schedule D (*De Beers Consolidated Mines v. Howe* (1906), A.C. 455). If the business is resident and controlled abroad, then persons resident in this country receiving profits from the business will be assessed under Case V. "Control," like "residence," is a question of fact.

In § 65 of the Report of the Income Tax Codification Committee it is stated :

"In addition to the principle that a company can have more than one place of residence, the case law on the subject of residence of companies seems to establish the following principles :—

(1) a company controlled in the United Kingdom is resident in the United Kingdom ;

(2) in the case of a British registered company, the establishment of a registered office in the United Kingdom and compliance with the other statutory obligations is not, of itself, sufficient to establish residence (*see Todd v. Egyptian Delta Land and Investment Co.* (1929), A.C.1; 14 T.C. 119) ;

(3) registration, though not of itself a sufficient test of residence, is a circumstance, and a strong circumstance, to be taken into consideration, and, if coupled with other activities in the country of registration, may well lead to the conclusion that the company is resident in that country (*Cesena Sulphur Co. v. Nicholson* (1876), 1 Ex.Div. 428; 1 T.C. 88; *Swedish Central*

*Railway Co. v. Thompson* (1925), A.C. 495 ; 9 T.C. 342) ;

(4) the test to be applied in the case of a foreign company cannot be different from that applicable in the case of a British company (*Todd v. Egyptian Delta Land, etc., Co. (supra)*)."

A finding by the Commissioners of Income Tax that a company which is registered abroad is resident in the United Kingdom for the purposes of assessment to Income Tax, on the ground that the control and directing powers of the company are in England is, if there is evidence to support it, conclusive, provided always that the Commissioners place the correct interpretation on the evidence (*American Thread Co. v. Joyce* (1913), 29 T.L.R. 266).

The establishment of a branch in the United Kingdom merely for the purpose of buying goods for export to the country where the profits are made does not bring a foreign firm controlled abroad into Case I. Only profits remitted to the resident partner are assessable under Case V (*Sulley v. Attorney-General* (1860), 2 T.C. 149).

Where the real control and management are situated is a question to be determined in each case according to the facts. Many cases have gone to the Courts on the point, each depending on its own facts. It is clear that if the controlling board of directors is in the United Kingdom, the company is resident therein, but if the board in this country is merely subsidiary to the local board, the local board is in control.

If the company resident in the United Kingdom carries on its foreign business through the agency of a foreign company which it effectively controls, the



British company is liable on the whole profits of the agent (*Apthorpe v. Peter Schoenhofen Brewing Co.* (1899), 4 T.C. 41). Control as a shareholder, without any interference in management, does not constitute effective control, and Case V applies, *i.e.*, only dividends are assessable (*Kodak v. Clark* (1903), 4 T.C. 549), even if the British company owns all the shares in the foreign company (*Stanley v. Gramophone & Typewriter Co.* (1908), 5 T.C. 358).

**(g) Profits earned in the United Kingdom by persons not resident therein.**

Any person trading in this country as distinct from trading with persons in it, is assessable on the profits made here. The machinery for collecting the tax is provided as follows :—

Any person not resident in the United Kingdom, whether a British subject or not, is charged in the name of any factor, agent or receiver having the receipt of any profits belonging to such person, in the same manner and to the same amount as would be charged if such person were resident in the United Kingdom, and in the actual receipt thereof (General Rule 5).

Any factor, agent or receiver so assessed may retain tax so paid out of moneys of his principal which come to his hands (General Rule 14).

This Rule is intended to aid the Commissioners in recovering the tax and not to alter the incidence of taxation in any way ; if the principal can be reached there is no need to have recourse to Rule 5 (*Tischler & Co. v. Apthorpe* (1885), 2 T.C. 89) ; in this case the judge indicated that as Mr. Tischler was in the United Kingdom some four months in the year he was capable of being served with the prescribed statutory notices, and was the proper person to return the profits made by exercising trade within the United Kingdom.

Whether a trade is exercised in this country turns primarily upon the question whether contracts in the course of trade are made in this country (*Rowson*

*v. Stephen* and *v. Commissioners of Inland Revenue* (1929), 14 T.C. 543), but even if contracts are made abroad, trade may in some circumstances be carried on in the United Kingdom (*Muller & Co. v. Lethem* (1927), 13 T.C. 126).

The Report of the Income Tax Codification Committee instances the following cases :—

(1) A foreign actor comes regularly, season after season, to act in London. Although resident for Income Tax purposes in the United Kingdom, he would not be treated as liable on any professional profits earned elsewhere than in the United Kingdom.

(2) An English doctor practises abroad as well as in the United Kingdom. He would be taxed on his profits earned abroad as well as on those earned in the United Kingdom.

(3) A foreign dressmaker (an individual) has a shop in London, and comes to London regularly to look after his London business. It is conceived that under the existing law and practice, no attempt would be made to tax him on his foreign profits, although he would be technically resident in the United Kingdom.

#### (h) Method of Assessment of Non-Residents.

Profits resulting from carrying on business in the United Kingdom must be ascertained according to the rules of the Income Tax Acts, and for this purpose accounts are required in the ordinary manner, in order to ensure that goods sent to this country for sale shall not be invoiced to this country at such price that all the profit thereon is made in the foreign country, no profit being made in this country.

Non-resident persons are chargeable to Income Tax in the name of any trustee, etc., or of any factor, agent, receiver, branch or manager; although the factor, agent, etc., may not have the receipt of the profits of the non-resident (General Rule 5).

A non-resident person may be charged in respect of any profits arising, whether directly or indirectly, through or from any branch, agency, etc., and is chargeable in the name of the branch, factor, agent, receiver or manager (General Rule 6).

Where a foreign manufacturer sells his products in this country, he makes a profit which consists of two parts, viz., a manufacturing profit and retailing profit. The manufacturing profit would be made in any case on a sale to someone in this country or elsewhere, and it is equitable that only the retail profit should be regarded as made by trading in the United Kingdom. Accordingly, where a non-resident is chargeable in respect of profits arising from goods or produce manufactured or produced by him outside this country, but sold here, the person in whose name he is chargeable may apply to the Commissioners by whom the assessment is made (or, in case of an appeal, to the General or Special Commissioners), to have the assessment made or amended on the basis of the profits which might reasonably be expected to have been earned by a merchant or, where the goods are retailed by or on behalf of the manufacturer or producer, by a retailer of the goods sold who had bought from the manufacturer or producer direct, and, on proof to the satisfaction of the Commissioners concerned of the amount of the profits on that basis, the assessment will be made or amended accordingly (General Rule 12).

**Illustration.**

The profits of a non-resident manufacturer on sales of his goods through an agent in the United Kingdom amounted to £6,000. It was shown to the satisfaction of the Commissioners that if the agent were a merchant purchasing the goods from the manufacturer for resale, his profits thereon would have been £3,200 only. The assessment will be amended to that figure, thus eliminating the manufacturing profit included in the £6,000.

If a non-resident person, not being a British subject or a British, Indian, Dominion, or Colonial firm or company, or branch thereof, carries on business with a resident person, and it appears to the assessing Commissioners that, owing to the close connection between the resident and the non-resident person, and to the substantial control exercised by the non-resident over the resident, the course of business between those persons can be so arranged, and is so arranged, that the business done by the resident, in pursuance of his connection with the non-resident, produces to the resident either no profits, or less than the ordinary profits which might be expected to arise from the business, the non-resident person shall be chargeable to Income Tax in the name of the resident person as if the resident person were his agent (General Rule 7).

Where it appears to the assessing Commissioners (or on appeal, to the General or Special Commissioners), that the true amount of the profits of any non-resident person chargeable to tax in the name of a resident person, cannot be readily ascertained, the Commissioners may, if they think fit, assess the non-resident person on a percentage of the turnover of the business done by the non-resident through or with the resident in whose name he is chargeable. In such case returns are required of the business done by the non-resident through or with the resident.

The percentage must be determined, having regard to the nature of the business, by the Commissioners by whom the assessment on the percentage basis is made, subject, in the case of an assessment made by the Additional Commissioners, to objection or appeal to the General or Special Commissioners.

If either the resident or non-resident person is dissatisfied with the percentage determined, either in the first instance or on appeal, he may, within four months of that determination, require the Commissioners to refer the question of the percentage to a Referee or Board of Referees to be appointed for the purpose by the Treasury, and the decision of the Referee or Board is final and conclusive (General Rule 9).

A non-resident person cannot be rendered chargeable in the name of a broker or general commission agent, or in the name of an agent who is not an authorised person carrying on the non-resident's regular agency, in respect of profits or gains arising from sales or transactions carried out through such a broker or agent (General Rule 10).

This rule is extended to provide that a non-resident shall not be chargeable in the name of a broker even though the broker acts regularly for the non-resident, provided the broker is carrying on *bonâ fide* the business of a broker, and that he receives remuneration at a rate not less than the customary rate in the class of business concerned. The term "broker" includes general commission agent (§ 17—1925).

The non-resident in such a case is not relieved of liability to tax on the profits made in this country, but the tax cannot be assessed upon the broker acting for him. If, however, the non-resident principal can

be reached, *e.g.*, on a visit to this country, he will be assessed in respect of the profits arising from sales conducted by brokers on his behalf.

The fact that a non-resident person executes sales or carries out transactions with other non-residents in circumstances which would make him chargeable in pursuance of the above rules in the name of a resident person, shall not of itself make him chargeable in respect of profits arising from those sales or transactions (Gen. Rule 11).

(i) **Foreign Companies earning profits partly in and partly outside the United Kingdom.**

A foreign company which earns part of its profits in the United Kingdom, will be assessed upon that part in the ordinary way (*Erichsen v. Last* (1881).

It had been held that where a non-resident company pays dividends to British shareholders, such dividends were chargeable to tax in full, notwithstanding that the profits out of which they are paid included dividends on shares held by the non-resident company in British companies, which dividends had already borne British tax; no abatement was allowed in respect of the proportion of the income already charged to British tax (*Canadian Eagle Oil Co. v. R*; *Selection Trust v. Devitt* (1945), 200 L.T.N. 61), over-ruling *Gilbertson v. Fergusson* ((1881), 7 Q.B.D. 562). (See also *Barnes v. Hutchinson* (1939), 18 A.T.C. 165.)

This position has now been put right for 1945-46 onwards.

If a dividend is paid by a body corporate not resident in the United Kingdom, and the "relevant profits" include profits on which United Kingdom Income Tax has been paid by that body corporate, by deduction or otherwise, a shareholder who receives

an ordinary dividend can claim relief (for 1945-46 onwards) in respect of a fraction of the dividend (§ 31—1946).

The relevant profits are as follows:—

- (a) If the dividend is paid for a specified period, the profits of the body corporate of that period ;
- (b) if the dividend is not for a specified period, but is paid out of specified profits, those profits ;
- (c) if the dividend is paid neither for a specified period nor out of specified profits, the profits of the last period for which accounts were made up which ended before the dividend became payable.

Should the total dividend exceed the profits of the period in (a) or (c), there is added to the profits of the period, so much of the most recent profits of previous periods (not previously distributed or regarded as relevant profits) as is necessary to make up the total dividend ; and where only part of the profits of any period are taken into account, that part is treated as consisting of profits on which United Kingdom tax has been paid of an amount which bears to the total profits of that period on which United Kingdom tax has been paid the same proportion as the part of the profits so taken into account bears to the whole profits of the period.

The fraction of the dividend is as follows:—

NUMERATOR: the gross amount of the relevant profits of the body corporate on which United Kingdom Income Tax has been paid by it, by deduction or otherwise.

DENOMINATOR: the said gross amount plus the gross amount of the relevant profits on which

United Kingdom Income Tax has not been paid by it.

The said gross amounts, however, are adjusted as follows :—

- (a) If by reason of the payment or charge of United Kingdom Income Tax, the body corporate has become entitled to deduct and retain tax on the whole or any part of any rent, interest, annuity or other annual payment, the gross amount of such rent, etc., from which tax is deducted, is to be deducted in arriving at the gross amount of the income that has suffered United Kingdom tax ;
- (b) any other rent, annual payment or royalty paid out of the relevant profits is to be deducted from the gross amount of the income on which United Kingdom tax has not been paid.

“ Gross amounts ” are the profits before deducting any Income Tax of any country.

Where a body corporate not resident in the United Kingdom controls, directly or indirectly, not less than half the voting power of any other body corporate not resident in the United Kingdom, and receives an ordinary dividend from that other body corporate, and the paying body has suffered United Kingdom tax, the receiving body is treated as having paid United Kingdom tax on the appropriate fraction of that dividend.

An ordinary dividend for the above purposes is a dividend on a share which is not a preferred share and so much of a dividend on a preferred share as is not paid at a fixed gross rate per cent.

The claim may be made at any time within six years after the end of the year of assessment.



The claim does not reduce the total income of the taxpayer, but in considering for the purposes of Gen. Rules 19 and 21 whether an annual payment is made out of profits brought into charge to tax, so much of the dividend as is the subject of relief under the claim is not treated as having been brought into charge.

#### Illustration.

A foreign company had the following profits for 1945-46 :  
From trading in the United Kingdom £10,000, from trading abroad £52,000. It declared a dividend on ordinary shares of £30,000, of which a shareholder received £1,400.

The company paid annual interest in the United Kingdom of £2,000, and abroad £4,000.

The shareholders can claim relief on—

$$\frac{£10,000 - £2,000}{(£10,000 - £2,000) + (£52,000 - £4,000)} \times £1,400 = £200$$

If United Kingdom tax had been deducted by the company, he can reclaim tax on the £200 ; if not, he will be relieved on his Case V assessment, or if he has already paid the tax, have the tax repaid.

## CHAPTER VI.

## BUSINESS PROFIT AND LOSS ACCOUNTS.

## § 1.—The Preparation of Accounts.

The method of adjusting the accounts of businesses in accordance with the rules and regulations of Income Tax has already been shown, and various items which are respectively allowed and disallowed have been stated, in connection with the accounts of sole traders, partnerships, and limited companies generally.

Some special cases, however, have particular features which it is thought advisable to illustrate separately in this chapter.

The professional accountant, in preparing accounts for Income Tax purposes from books which he has not himself audited, must be careful to scrutinize the actual accounts in the books, in order that he may judge whether the amounts included in the balances on the various accounts are precisely described by the accounts themselves.

## § 2.—Banks.

Any bank carrying on a *bonâ fide* banking business in the United Kingdom is relieved from Income Tax under Schedule C on interest in respect of all subscriptions to war loans issued for the purposes of the 1914-18 War (Rule 3, General Rules, Sch. C), and in place thereof the interest on such loans is assessed under Case I, Schedule D (Rule 14, Cases I and II, Sch. D).

This method enables a bank to charge its expenses against such interest in cases where there would otherwise have been an adjusted loss.

It may be mentioned that the Commissioners interpret this section somewhat strictly, and the mere registration of a person or a company as a banker will not in itself be sufficient to obtain the benefit of the clause.

The following is a representative example of the adjustments involved in a bank computation.

INCOME TAX COMPUTATION.

Net Profit per Profit and Loss Account..	..	£450,000
Add Transfers to Reserve .. .. .	..	100,000
Profits on Sale of Investments carried to Reserve .. .. .	..	15,600
Depreciation on Investments .. .. .	..	1,400
Income Tax, etc., Depreciation and other disallowable charges .. .. .	..	139,000
		<hr/>
		706,000
<i>Deduct</i>		
Net Annual Value of Bank Premises ..	£41,000	
Loss on Sale of Investments carried to Reserve .. .. .	3,000	
Income Taxed at Source .. .. .	218,000	
		<hr/>
		262,000
		<hr/>
Adjusted profits .. .. .	£444,000	
(Subject to deduction of P.T.)		

It should be noted that dealing in investments is considered as part of a bank's trading transactions.

### § 3.—Breweries.

#### *Tied House Expenditure.*

A tied house is one held by the brewers as freeholders or leaseholders which is let to tenants on the understanding that they shall sell only the particular beers manufactured by the brewers concerned. The brewer is allowed to charge in his accounts :—

- (a) Repairs executed for the purpose of trade.
- (b) The excess of the gross Schedule A assessments or rent paid (if greater) over the rents received from tied houses. If leasehold, the lease rent paid should be disallowed.
- (c) Fire and Licence Insurance Premiums, and legal and other expenses in connection with tied houses (*Usher's Wiltshire Brewery v. Bruce* (1914), 31 T.L.R. 104).

It was held in *Collyer v. Hoare & Co.* ((1932), 17 T.C. 169) that in determining the amounts to be allowed as deductions in respect of deficiencies of rent each tied house must be considered separately.

In *Collyer v. Hoare & Co.* ((No. 2) (1937), 21 T.C. 318), it was held that in determining the deficiency of rent, money *expended* in premiums on the acquisition of leases being like expenditure on improvements of a capital nature, could only be considered to the extent that it might increase the rack rent; the annual equivalents of such expenditure could not be treated as rent payable, but in computing the deduction for a particular tied house, account must be taken of any *premium received* as well as of rent.

Following this principle, if a brewery business is sold and the licensed house is regarded as part of the business premises, it matters not whether the owner of the business is the person who received the premium when the lease was granted, since that premium must be regarded as being received year by year during the currency of the lease. A brewery company which, during the currency of the lease, acquires the tied house must be deemed to be in receipt year by year of the appropriate part of the premium which was actually received by the person who owned the business

when the lease was granted (*Lucas v. Charles Hamerton & Co.* (1944), T.R. 223).

### *Compensation Levy.*

Compensation levy payable under the Licensing Act, 1904, is also allowed, on the ground that the payment is essential to the earning of profits, and not a deduction from the profits after they are made (*Smith v. Lion Brewery Co.* (1911), 27 T.L.R. 261).

The following are not allowed as deductions for Income Tax purposes :—

(1) Premium paid on lease of tied house (*Watney v. Musgrave* (1880), 42 L.T. 690).

(2) Damages and costs recovered by a guest injured by the fall of a chimney while sleeping in an hotel, on the ground that such loss was not connected with or did not arise out of the trade (*Strong & Co., Ltd. v. Woodfield* (1906), A.C. 448).

(3) Cost of application for new licences (*Southwell v. Savill Bros.* (1901), 2 K.B. 349).

(4) Instalments in respect of monopoly value (*Kneeshaw v. Abertolli* (1940), T.R. 391; *Henriksen v. Grafton Hotel* (1942), T.R. 105).

### **Illustration.**

The following is the Trading and Profit and Loss Account of a Provincial Brewery Company for the year ended 31st December, 1945.

Wear and Tear Allowance for the fiscal year 1946-47 is admitted at £1,600.

The gross values for Schedule A of the tied houses amount to £21,210, and the actual rents received therefrom amount to £20,000. Included in these rents were amounts totalling £3,500 in respect of certain tied houses assessed for Schedule A at a gross value of £3,200. No premiums had been received.

The net Schedule A value of the Brewery is £2,400. For rating £2,000.

Show the Income Tax Assessment for the year 1946-47.

## Dr. TRADING AND PROFIT AND LOSS ACCOUNT, YEAR ENDED 31ST DEC., 1945. Cr.

To Stock .. .. .	£ 9,548	By Beer Sales .. .. .	£ 99,104
" Purchases .. .. .	23,000	" Yeast and Grains .. .. .	900
" Beer Duty .. .. .	10,000	" Stock .. .. .	10,000
" Beer Purchased .. .. .	7,000		
" Coal .. .. .	1,000		
" Wages .. .. .	3,700		
" Gross Profit .. .. .	49,756		
	<u>£110,004</u>		<u>£110,004</u>
To Pensions .. .. .	£ 946	By Gross Profit .. .. .	£ 49,756
" Rates, Electric Light, etc. .. .. .	900	" Commissions .. .. .	1,800
" Horse Keep and Motor Expenses .. .. .	1,500	" Rents Receivable on	
" Tenants' Rates .. .. .	250	Licensed Properties .. .. .	£20,000
" Tenants' Licences .. .. .	500	Less Rents Payable .. .. .	10,500
" Company's proportion of Extra			9,500
Licence Duty .. .. .	6,000	" Interest on Loans to Tenants (less	
" Loans to Tenants irrecoverable .. .. .	1,000	Tax) .. .. .	1,715
" Bad Debts .. .. .	800	" Transfer Fees .. .. .	10
" Licences (Brewery and Stores) .. .. .	100		
" Charitable Donations .. .. .	280		
" Fire Insurance, Brewery and Premises	400		
" Law Costs, Tenants' Agreements, etc. .. .. .	200		
" Salaries .. .. .	1,400		
" Discounts .. .. .	600		
" Advertising .. .. .	500		
" Loss on Managed Houses .. .. .	200		
" Repairs to Licensed Premises .. .. .	1,850		
" Compensation Levy .. .. .	2,000		
" Repairs to Brewery and Plant .. .. .	1,500		
" Directors, Trustees and Auditors .. .. .	3,000		
" Interest on Debentures and Loans .. .. .	15,000		
" Depreciation of Plant .. .. .	1,000		
" " Lenses .. .. .	2,500		
" " Casks, Drays, etc. .. .. .	1,000		
" Bank Interest .. .. .	120		
" Net Profit .. .. .	19,235		
	<u>£62,841</u>		<u>£62,841</u>

## INCOME TAX COMPUTATION.

Net Profit .. .. .	£19,235
Add: Interest on Debentures and Loan .. .. .	15,000
Depreciation of Plant .. .. .	1,000
" Leases .. .. .	2,500
" Casks, Drays, etc. .. .. .	1,000
Profit Rentals .. .. .	300
	<u>39,035</u>
Deduct: Rents Receivable on Licensed	
Properties (less Rents Payable) .. .. .	9,500
Interest on Loans to Tenants .. .. .	1,715
Schedule A value of Brewery (net) .. .. .	2,400
Factory depreciation, $\frac{1}{8}$ th of £2,000 .. .. .	400
	<u>14,015</u>
Carried forward .. .. .	£25,020

Brought forward ..	£25,020
<i>Less:</i> Excess of Gross Schedule A Values of Tied Houses where this exceeds the rent receivable, over the rent receivable therefrom (£21,210-3,200) — (£20,000-3,500) .. .. .	1,510
	<hr/>
	23,510
<i>Less</i> Wear and Tear .. .. .	1,600
	<hr/>
Assessment 1946-47 .. .. .	£21,910
(Subject to deduction of N.D.C. or E.P.T.)	<hr/>

*Notes.*

- (1) TENANTS' RATES AND TENANTS' LICENCES; LAW COSTS, TENANTS' AGREEMENTS, ETC.; REPAIRS TO LICENSED PREMISES.

These are allowed as a charge (*Usher's Wiltshire Brewery Co., Ltd. v. Bruce* (1914), 31 T.L.R. 104).

- (2) COMPANY'S PROPORTION OF EXTRA LICENCE DUTY.

It is assumed that this charge has been placed upon the company by the Commissioners in accordance with § 46 of the Finance (1909-10) Act, 1910, and will therefore be allowed as a charge.

- (3) ADVANCES TO TENANTS IRRECOVERABLE.

This item is allowed if the loan was originally represented by money advanced (*Reid's Brewery Co. v. Male* (1891), 2 Q.B. 1); but if, as in the majority of transactions of this nature, cash does not pass, the item will not be allowed. It is assumed here it was an actual cash transaction.

- (4) CHARITABLE DONATIONS.

These are assumed to be allowed as annual contributions to hospitals from which the employees and their dependants may derive benefit.

- (5) RENTS RECEIVABLE LESS RENTS PAYABLE.

This item represents the difference between rents received on freehold and leasehold licensed properties and rents paid in respect of them. Both these items being taxed under Schedule A, the difference between the two can be written back for Income Tax purposes.

## (6) RENTS.

The brewer is allowed in respect of tied houses to deduct from his assessment the excess of the gross Sch. A values of tied houses over the net rents received from them where there is such an excess. Prior to 1940-41, if the rent receivable in respect of any house exceeded the gross Sch. A value, the excess was not taxable (*Collyer v. Hoare & Co.* (1932), 17 T.C. 169). The trading profit is reduced by the amount of the loss sustained in respect of rents of properties tied to the trade and therefore let at what is frequently a nominal or, at any rate, an uneconomic rent (*Usher's Wiltshire Brewery Co. v. Bruce, supra*). Profit rentals are now taxable (1940-41 onwards) (see Chap. III, § 1 (g)). Since repairs are charged, the gross excess rent is kept in credit avoiding a Case VI assessment.

## (7) FACTORY DEPRECIATION.

The allowance is restricted to one-fifth of the net annual value for rating, since the brewery is outside London. As from 6th April, 1946, the company could claim to have the Annual Allowance granted under the Income Tax Act, 1945, substituted for the Factory Depreciation Allowance. Even though no such claim is made, the Factory Depreciation Allowance will cease in 1950-51, and the Annual Allowance will be given from 1951-52 onwards.

## § 4.—Builders.

The adjustment of accounts in the case of builders follows the usual rules, but the following points must be noted:—

- (1) Work in progress must be valued according to sound accountancy principles, and the same basis be adopted from year to year. No portion of anticipated profit need be included.
- (2) Engines, cranes, etc., are machinery and plant on which a Wear and Tear Allowance can be claimed, but ladders, scaffolding, ropes, etc., are dealt with on a renewals basis.



- (3) Where houses are sold subject to a "ground annual" (the Scottish equivalent of a rent-charge), the realisable value of the ground annuals must be treated as part of the sale price and brought into credit in arriving at the profits (*John Emery & Sons v. C.I.R.* (1936), 20 T.C. 213). If, however, a house is let or sold leasehold, only the premium for the lease need be brought into account, ignoring the value of the ground rent; there is no realisation of the freehold and the value of the reversionary interest cannot be brought into computation (*Hughes v. B.G. Utting & Co.* (1940), T.R. 175).

The difference between the two cases is, that in the *Emery* case the builder had ceased to be the owner of the house and ground and became the owner of a rent charge, whereas in the *Utting* case he continues to be the owner of the house and ground, though a partial interest in the house has been sold, and his ownership is subject to that interest. The cost price only of the ground rent has to be carried forward, and when the ground rent is sold, the proceeds will be brought into credit in the accounts of the period covering the date of realisation (*Utting* case). The development expenses (land, levelling, clearing, roads, sewers and a fair addition for building costs) should be apportioned as nearly as possible between the leasehold properties constructed and the ground rents created, the latter proportion being carried forward in adjusting the accounts of the business of property development.

Where a house is sold for a lump sum and for a feu duty payable by the purchaser, the cost is to be computed as that proportion of the total expenditure in acquiring the land, developing it and erecting houses on it, which the lump sum bore to the total amount made up of the selling value of the feu duty (the price prevailing at the date of its creation) and the lump sum (*McMillan v. C.I.R.* (1942), T.R. 183).

- (4) In order to facilitate the sale of houses, it is common for builders to make an arrangement with a Building Society under which the Society advances to the purchaser nearly all the purchase price, the builders guaranteeing to the Society a proportion of the advances and making also a deposit with the Society of about one-third of the sum guaranteed (on which interest is allowed by the Society). In such cases, the amount of the deposits is deducted from the sale price of the houses for the purpose of arriving at the profits. The deposits must then be brought into credit at their present value having regard to the contingency of loss. If, however, the Commissioners find that such a valuation is impracticable, the deposits should be treated as receipts of the company's trade, only in so far as they are released to the company in the accounting period (*Harrison v. Cronk & Sons* (1936), 20 T.C. 612). As a proper actuarial valuation is invariably impossible, it is the practice to adopt the second method, i.e., to bring into

credit the amounts released in the trading period.

The above principle was followed in a case where the builder takes from the purchaser a second mortgage or promissory note for the balance of the price after deducting the deposit and the amount advanced by the building society on the first mortgage. The debts which represent the outstanding portions of purchase money which will be received in subsequent years must be valued (*Absolom v. Talbot* (1944), T.R. 195).

### § 5.—Doctors.

Medical men's accounts present little difficulty except in the following respects:—

- (a) They are often kept on a "cash basis," i.e., although all expenditure is charged on an accruals basis, only those fees actually received in cash are brought into credit. "When a trader or follower of a profession or vocation dies or goes out of business.....and there remain to be collected sums owing for goods supplied during the existence of the business or for services rendered by the professional man during the course of his life or his business, there is no question of assessing those receipts to Income Tax; they are the receipts of the business while it lasted; they are the arrears of that business; they represent money which is earned during the life of the business, and are taken to be covered by the assessment made during the life of the business, whether that assessment was made on the basis of bookings or on the basis of receipts" (Rowlatt, J. in *Bennett v. Ogston*

(1930), 15 T.C. 374). In the case of new practices, the Inland Revenue will not usually countenance the adoption of the cash basis, but insist on the preparation of proper Income and Expenditure Accounts. It is, however, a matter for the Commissioners to decide whether a cash account is acceptable.

- (b) A proportion of the net annual value of, or the rent paid for, the doctor's residence, is properly chargeable. This proportion should be fixed having regard to the fact that a medical man must maintain a much larger house than would be necessary for his personal use, in order to attract patients. Although he may only use two rooms for his practice, he should be allowed a proportion higher than the mere value of such rooms. A proportion of the cost of lighting, heating, cleaning, and of servants' wages should also be allowed.
- (c) The major portion of the cost of running his motor car is chargeable to the practice. An account of all expenses should be kept and charged, a reasonable portion being added back for private use.\* The wear and tear and obsolescence allowances must be apportioned on a similar basis. If a new car is purchased every year, the renewals basis is more satisfactory. In London, taxi fares are commonly considerable in the case of specialists with hospital appointments.
- (d) The salary of a *locum tenens* employed during a vacation or illness will usually be allowed as a deduction.

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\*There will, of course, rarely be private use during the petrol restrictions.

- (e) It is common for doctors who are in partnership to agree that certain expenses shall be regarded as joint expenses, to be deducted from the income in arriving at the profit for division, and for any other expenses incurred to be met by each partner out of his share so ascertained. Care must be taken to divide the assessment on this basis, *i.e.*, individual expenses will be added, the total divided, and these expenses deducted again in a manner similar to the adjustment for salaries and interest on capital in trading partnerships.

## § 6.—Farmers.

The following points require attention in the case of farmers :—

### (1) *Farmer's Valuations for Income Tax.*

As a result of meetings between representatives of the Agricultural Departments, the Inland Revenue, and the Farmers' Unions on the subject of valuations for Income Tax purposes, an agreement was reached of which (iii) below has been given statutory effect in § 67 and 10th Sch., 1947.

#### (i) **Valuation of tillages, unexhausted manures and growing crops.**

It has been agreed by the Inland Revenue Department that, subject to the concurrence of the District Commissioners of Taxes—

- (a) Where the normal value of tillages, unexhausted manures and growing crops does not exceed £700, and a detailed valuation is not available, a certificate that the value at the beginning of the year did not differ materially from that at the end of the year will usually be accepted, and

- (b) Even where the normal value exceeds £700 a valuation will not be pressed for in every case, and a similar certificate may be accepted after any inquiry necessary to establish its reasonable accuracy.

The object of this arrangement is to assist farmers by enabling a detailed valuation to be dispensed with in such cases.

There is, however, nothing in the arrangement (which is in terms limited to cases where detailed valuations are not available) precluding a farmer, who so desires, from bringing into his accounts a full detailed valuation of tenant right or waygoing rights and liabilities at the beginning and end of year; any farmer who makes a detailed valuation is at liberty to put in that valuation and should, in fact, do so. The valuation should be made on precisely the same basis as if valuing an outgoing tenant. In other words, the valuation would, in the case of a tenant, be based upon the actual tenancy agreement and, in the case of an owner-occupier, be based on the custom of the country which would, in the absence of a written agreement, be applicable if a tenancy existed.

(ii) **Basis of valuation of live stock.**

The basis of valuation of live stock should be cost or market value, whichever is the lower. In the case of live stock bred on the farm, if it is not possible to ascertain the actual cost, no objection will be raised to the acceptance, as the cost valuation, of the market price less 15 per cent., this basis of valuation to apply both for the opening and closing figures of the year of account by reference to the market price at the opening and closing dates, respectively. Uniformity in the method of valuation should be aimed at, but where

The election must apply to all production herds of a particular class kept by the farmer, including herds which he has ceased to keep before the making of the election, or first begins to keep thereafter.

Animals kept wholly or mainly for the work they do in connection with carrying on the farm cannot be included in a herd.

**(b) Definitions.**

The expression "herd" includes a flock and any other collection of animals, however named. "Animals" include any living creatures.

The expression "a production herd" means, in relation to a farmer, a herd of animals of the same species (irrespective of breed) kept by him wholly or mainly for the sake of the products which they produce for him to sell, being products obtainable from the living animal.

The expression "product obtainable from the living animal" means :—

- (i) the young of the animal ; or
- (ii) any other product obtainable from the animal, not being a product obtainable only by slaughtering the animal itself.

Production herds kept by a farmer are deemed to be of the same class if and only if all the animals kept in the herds are of the same species (irrespective of breed), and the products produced for him to sell for the sake of which (either wholly or mainly) the herds are kept by him, are of the same kinds in the case of all the herds : and elections for the herd basis shall be framed accordingly.

The provisions apply (with the necessary adaptations) in relation to animals kept singly as they apply in relation to herds, *e.g.*, a stallion, but not to any animal kept wholly or mainly for public exhibition or racing or other competitive purposes.

**(c) Immature animals.**

Immature animals kept in a herd are not treated as forming part of the herd unless—

- (a) the land on which the herd is kept is such that animals which die or cease to form part of the herd cannot be replaced except by animals bred and reared on that land ; and
- (b) the immature animals in question are bred in the herd, and are necessarily maintained therein for the purpose of replacement.

In what follows, references to an animal being added to a herd include references to an immature animal which is kept in the herd

becoming a mature animal, but not more immature animals can in any case be treated as forming part of a herd than are required to prevent a fall in numbers of the herd. Female animals are regarded as becoming mature when they produce their first young. Laying birds are treated as becoming mature when they first lay.

**(d) Effect of Election.**

Where an election has been made, the initial cost of the herd is not to feature in the Profit and Loss Account, but is regarded as capital. The same applies to the cost of any animal added to the herd, save as a replacement.

**(e) Additions to herd.**

If an animal is taken out of trading stock and added to a herd otherwise than as a replacement, there must be credited to Profit and Loss Account—

- (a) If the animal was bred by the farmer, the cost of breeding it and rearing it to maturity ;
- (b) If the animal was not bred, its initial cost to the farmer, plus the cost of rearing it to maturity.

**(f) Replacements.**

Where an animal forming part of a herd dies or is taken out of the herd, and is replaced, the sale proceeds of that animal must be credited to Profit and Loss Account, and the cost of the replacement debited except to the extent that such cost has already been allowed as an expense.

If, however, the replacement is of better quality than the animal replaced, it is only permissible to charge the amount that would have been expended to acquire an animal of the same quality ; if the animal replaced was slaughtered by an order from any Ministry or other authority under the law relating to diseases of animals, and the replacement is of worse quality, the amount included as a trading receipt is not to exceed the amount allowable as a deduction.

**(g) Replacement of whole herd.**

Where the herd is sold as a whole and another production herd of the same class is acquired, the above provisions apply as though there had been sold from the original herd, and replaced therein, a number of animals equal to the number in the original herd or in the newly acquired herd, whichever is the less. (See also (j) below.)

**(h) Sale of whole herd.**

If (either all at once or over a period not exceeding twelve months) either—

- (a) the whole of a herd is sold and not replaced ; or



- (b) a part of a herd is sold on a substantial reduction being made in the number of animals in the herd,

any profit or loss arising from the transaction is not to be taken into account. This is subject to the proviso that where, within five years of the sale, the seller either acquires or begins to acquire another production herd of the class in question or acquires or begins to acquire animals to replace the part of the herd in question—

- (i) The above provisions regarding replacement ((f) and (g)) apply to the acquisition or replacement, except that if the sale was one which the seller was compelled to effect by causes wholly beyond his control, the amount included as a trading receipt in respect of any animal sold which is replaced by an animal of worse quality, is not to exceed the amount allowable as a deduction in respect of the said animal of worse quality; and
- (ii) for the purposes of the application of those provisions, the proceeds of sale of the animals comprised in the original herd or part of a herd are to be brought into account as if they had been respectively received at the times of the corresponding acquisitions.

**(i) Other sales.**

If an animal forming part of the herd is sold and none of the three last paragraphs ((f), (g) or (h)) applies, any profit or loss arising from the transaction is to be included or deducted, as the case may be; for this purpose the profit or loss is to be computed by comparing—

- (a) in the case of an animal bred by the farmer, the cost of breeding it and rearing it to maturity; and
- (b) in any other case, a sum equal to the initial cost to the farmer of acquiring the animal (or, in the case of an animal acquired otherwise than for valuable consideration, its market value when it was acquired by the farmer) together, in both cases, with any cost incurred by him in rearing it to maturity,

with the proceeds of the sale.

**(j) Sale of whole herd and purchase of slightly smaller herd.**

Where the herd is sold as a whole, and another production herd of the same class is acquired, and the number of animals in the newly acquired herd is less than the number in the original herd, and the difference is not substantial, sub-paragraph (h) above shall not apply, but (i) above shall apply to a number of animals in the original herd equal to the difference.

**(k) Death or destruction of animals: value.**

The preceding provisions apply in relation to the death or destruction of animals as they apply in relation to the sale of animals,

as if any insurance or compensation moneys received by reason of the death or destruction thereof were proceeds of sale, and any references to the proceeds of sale of an animal include references to any proceeds of sale of its carcase or any part thereof.

**(l) Herd acquired more than five years after sale of herd.**

A farmer who, having kept a production herd of a particular class, ceases altogether to keep herds of that class for a period of at least five years shall, as respects production herds kept by him after the end of that period, be treated as if he had never kept any production herds of that class before the end of that period.

**m) Anti-avoidance provisions.**

Where a farmer transfers to another person all or any of the animals which form part of a production herd otherwise than by way of sale, or by way of sale but for a price other than that which they would have fetched if sold in the open market, and either—

- (a) the transferor is a body of persons over whom the transferee has control, or the transferee is a body of persons over whom the transferor has control, or both the transferor and the transferee are bodies of persons and some other person has control over both of them ; or
- (b) it appears with respect to the transfer, or with respect to transactions of which the transfer is one, that the sole or main benefit or one of the main benefits which, apart from the provisions of this paragraph, might have been expected to accrue to the parties or any of them was a benefit resulting from the obtaining of a right to make an election for the herd basis, or from such an election having effect or ceasing to have effect, or from such an election having a greater effect or a less effect,

then the like consequences ensue for all relevant tax purposes in relation to all persons concerned as would have ensued if the animals had been sold for the price which they would have fetched if sold in the open market.

For this purpose, the expression " body of persons " includes a partnership and the expression " control " has the meaning assigned to it by § 68 (1), Income Tax Act, 1945.

**(n) Application to other businesses.**

The above provisions, with the necessary adaptations, apply to trades other than farming.

**(o) Returns, assessments, etc.**

The Inspector of Taxes may require such returns as to, and as to the products of, the animals as he needs. If an election changes

the assessment for a year, additional assessments or repayments will be made to give effect to the change. Appeal in respect of a claim may be made to the General or Special Commissioners.

### Illustrations.

(1) A bull which cost £75 is replaced in the herd by one costing £200. It is necessary to decide whether the new bull is of similar type and quality to the old; if so, the sale price of the old bull will be credited to revenue and the £200 for the new bull debited. If, however, it is a better bull, and a bull of similar type could have been bought for £110, then £200 - £110 = £90 must be capitalised as an improvement, only £110 being debited to revenue, the sale price of the old bull being credited as before.

(2) A cow which cost £40 is sold out of the herd and not replaced, realising £35. The loss of £5 is charged to revenue.

(3) A farmer sells for £2,750 (at £55 a head) a herd of 50 animals which originally cost him £2,000. Six months later he buys a new herd of 45 animals of the same quality for £2,250.

	£	£
Sale price of 45 animals of old herd, to be credited to trading account ..		2,475
Cost of new herd of 45 animals, to be debited to trading account ..		2,250
		<hr/>
Net profit on sale of 45 animals		225
Sale price of 5 animals not replaced	275	
Cost price of 5 animals not replaced	200	
	<hr/>	75
Total (net) profit to be included		<u>£300</u>

(4) Animal slaughtered for foot and mouth disease and replaced by an inferior animal costing £50.

Compensation received £70.

There must be included in the accounts a debit of £50 for the new animal, but only £50 of the compensation need be brought into credit.

### (2) *Stud Farms.*

The usual method is as follows :—

(a) Both stallions and mares are to be dealt with as stock-in-trade and valued at the beginning and end of each year on the usual basis of cost or market value, whichever is the lower. (In

determining whether cost or market value is appropriate, all the animals must be taken as a single unit.)

(b) If an occupier of a stud farm races animals bred by him, the stud farm accounts are to be credited, when animals are transferred to training, with the then market value of the transferred animals as if they had been then sold at that value, and when animals return to the stud farm after racing, the stud farm's accounts are to be debited with their market value at the time of return as if they had then been purchased at that value. (If an animal purchased, and not bred on the stud farm, is brought into the stud after racing by the occupier, the stud farm accounts will similarly be debited with the then market value of the animal as if it had then been purchased at that value.)

(c) The same treatment would be regarded as applicable also to a person who is assessable under Sch. D in respect of the profits of dealing in thorough-bred animals bred by him but on a stud farm occupied by some other person.

(d) As regards the ordinary farming carried on on a stud farm, the occupier may claim the treatment of herds, etc., which is set out above.

### (3) *Rent, etc.*

A tenant farmer may deduct as an expense the rent of the land, farm buildings and farm cottages, and also of that part of the farm house (usually one-third) which is used for farming purposes. The balance of rent of the farm house is regarded as part of living expenses. If labourers are boarded, the proportion

of the rent of the house to be charged will be so much greater, of course, unless as is usual it is included in the charge for such board (*see* below).

An owner-occupier is allowed to deduct the net annual value in lieu of rent, with the same disallowance of that part of the farm house deemed to be domestic. The gross annual value (less proportion deemed to be domestic) is usually allowed if repairs etc., are dealt with by maintenance claims. Unless dealt with by way of a maintenance claim under Sch. A, the following are deductible : (a) repairs (including the proportionate part of those of the farm house) ; (b) the interest portion (five-sixths) of the Redemption Annuity (if any) payable under the Tithe Act, 1936 ; (c) land tax ; (d) public drainage rates. In Scotland, stipend is not deductible, it is treated as an annual charge.

(4) *Wages, etc.*

The cost of board of workers living in the house is deductible. This may be taken as the difference between the wages actually paid and the wages that would be payable if they were not boarded, or may be calculated more exactly. Servants wholly employed in the household must be excluded, but in the case of any partly employed on the farm, the proportionate wages and keep are deductible.

As the rent or annual value of cottages is deductible, it must not be included again in wages ; any rent received must be included in profits.

Wages to the wife or other members of the family must be reasonable and actually paid.

(5) The following interest is paid gross : on advances under the Agricultural Credits Act, 1923 ; or from the Agricultural Mortgage Corporation Ltd., or the Scottish Agricultural Securities Corporation.

(6) The ploughing grant received for ploughing up grassland is a revenue receipt (*Higgs v. Wrightson* (1944), T.R. 49).

(7) *Relief under the Income Tax Act, 1945* (§§ 32-34).

As from 6th April, 1946, relief is given (in the same way as wear and tear allowances) to owners and tenants of agricultural or forestry land and buildings, in respect of capital expenditure on buildings and works where the expenditure does not fall within a maintenance claim for Sch. A. The allowance is an annual one of one-tenth of the expenditure for each of the ten years following the year in which the expenditure was incurred.

The allowance is given to the owner or tenant according to which of them incurred the expenditure. To qualify for allowance, the land, etc., must be occupied wholly or mainly for the purpose of husbandry. Forestry land means woodlands in the United Kingdom assessed under Sch. D, and houses or other buildings occupied wholly or mainly for the purposes of the woodlands. The expenditure must be on construction, reconstruction, alteration or improvement of farm houses, farm or forestry buildings, cottages, fences or other works, *e.g.*, drainage and sewerage works, water and electricity supply installations, walls, shelter belts of trees, reclamation of former agricultural land, etc.

The expenditure must have been incurred on or after 6th April, 1944, but there must be deducted from expenditure between that date and 6th April, 1946, any exceptional depreciation allowed. (Such expenditure is deemed to be incurred on 6th April, 1946, and will rank for allowances for 1947-48 to 1956-57.)

In the case of a farm house, only one-third of the expenditure qualifies for relief, or if the house is unduly large in proportion to the nature and extent of the farm, a smaller fraction. If any asset serves also some purpose other than husbandry or forestry, an apportionment is necessary between the purposes.

Grants from the Crown, local authorities, etc., must be deducted from the expenditure. Grants by a landlord will entitle the landlord to relief thereon. In other cases, the landlord or tenant will get relief in full (according to which of them provided the buildings, etc.) despite a contribution from a person other than the Crown or other authority (§ 66—I.T.A. 1945).

The allowances will be based on the expenditure to 31st March preceding the year of assessment, unless the claimant agrees some other date (*e.g.*, his accounting date) with the Inspector of Taxes.

The allowances are given primarily against agricultural or forestry income, *i.e.*, the Sch. B or D assessment on the farm; excess rents and rent in the case of the landlord; Sch. A and Sch. D and excess rents in the case of woodlands. Any excess allowance may be carried forward, or may be set against other income, if claimed within 12 months after the end of the year of assessment (§ 56—I.T.A. 1945).

If the person who incurred the expenditure sells the land or transfers it in any other way, the allowances for years after the transfer go to the transferee. Where an outgoing tenant receives payment from the incoming tenant for the assets in question, the latter will get the remaining allowances from the date of transfer.

If, however, the incoming tenant pays nothing, the landlord will get the remaining allowances.

The above remarks apply to transfers of part of assets. A person buying assets gets no allowances except as above.

#### Illustration.

In 1945, a landlord built a new cottage, costing £1,100 on A's farm. In 1947 A spent £500 on capital extensions and improvements of the buildings.

The landlord will be entitled to an allowance of £110 a year for 1947-48 to 1956-57; the tenant to £50 a year from 1948-49 to 1957-58.

If the tenant transfers the farm to another farmer in 1950, the allowances for 1951-52 to 1957-58 will go to the incoming tenant, provided he pays for the improvements, otherwise the allowances revert to the landlord.

#### § 7.—Hotels.

The special items to be noted in the case of hotels are as follows :—

- (a) The cost of meals and maintenance of the staff and proprietor is usually credited to the Trading Account and debited as a specific charge either in that account or in the Profit and Loss Account. The proportion attributable to the proprietor is not an allowable item, being an appropriation of profit, and must be added back for Income Tax purposes.
- (b) A proportion of the rent or net annual value, whichever is chargeable, must be added back, in the case of a resident proprietor in respect of the portion of the hotel occupied by him and his family.
- (c) Any charge made in the accounts in respect of hire purchase instalments on furniture, etc., must be apportioned between interest charges, which are allowed, and part hire instalments, which must be added back.



- (d) A Wear and Tear Allowance should be claimed on furniture, etc., except in the case of those items which are subject to constant renewal through breakages, etc., on which the renewals basis should be adopted.

### § 8.—Savings Banks.

The income of savings banks which would be chargeable under Schedules C or D is exempt from tax in the year for which exemption is claimed so far as the income is applied in the payment or credit of interest to any depositor. (The interest is chargeable on the depositor under Case III, Schedule D.)

In any case, however, where the interest paid or credited to any depositor exceeds £15, the bank or branch concerned must make a return to the Inspector of Taxes for the district in which it is situated of the names and addresses of such depositors, otherwise it will not obtain the relief to which it is entitled by this section.

Any such return must be made before the 1st of May in the year following that in respect of which exemption is claimed (§ 39 (3); § 32—1920; § 24—1924).

A savings bank may claim repayment of tax in respect of management expenses (§ 33—see Chap. IX, § 7).

### § 9.—Private Schools.

The schoolmaster himself generally occupies a portion of the school premises, and if he is the proprietor, only a proper proportion of the rent (or net annual value) can be deducted in arriving at the profits. This will be not more than two-thirds, unless the Commissioners are satisfied that a greater proportion ought, in the circumstances, to be deducted

(Rule 3 (c), Cases I and II, Sch. D; § 31—1921). If the proprietor does not live on the premises, the full rent or net Schedule A assessment can be charged.

In the same way, if the proprietor lives on the premises it is necessary to apportion the various classes of expenditure, such as rates, lighting, etc., as only the part applicable to and necessary for the business can be allowed as a charge, and the usual procedure is to treat this proportion as two-thirds of the whole, except in the case of a large school, when a greater proportion may be allowed. The estimated cost of meals, etc., for the proprietor and his family must be disallowed as a deduction.

By concession, wear and tear allowance may be claimed on school furniture and fixtures.

### § 10.—Lloyd's Underwriting Syndicates.

The following is an illustration of the method of arriving at the assessable profits of an underwriting syndicate :—

#### Illustration.

X is an underwriter and underwriting agent at Lloyd's, who balances his books regularly on the 31st December of each year. He writes for himself and three names, viz., A, B, C; for himself and A a double line, and a single line for B and C. His accounts are kept in syndicate form.

You are required to adjust the syndicate accounts for Income Tax purposes, and allocate the underwriting profits between the members of the syndicate to enable them to fill up correctly their Income Tax Returns for 1947-48, in so far as the underwriting profits are concerned.

The charges represent a salary to X which is at the rate of £200 per annum per name. X also receives as agent a commission of 10 per cent. on the ascertained net profits from each name after charging Profits Tax (N.D.C.). He charges against his own account salary and commission in exactly the same manner as he does against the accounts of his names. (Assume Profits Tax (N.D.C.) £300.)

The Underwriting Agent X will be liable to assessment in respect of the salary and commission after charging any admissible expenses which have not been debited in the Underwriting Accounts.

The following is the Underwriting Account for the syndicate of X and others for the year 1946, closed in 1948 :—

## X AND OTHERS.

<i>Dr.</i>		UNDERWRITING ACCOUNT FOR THE YEAR 1946.				<i>Cr.</i>	
1946. Dec. 31	To Claims .. ..	£	s. d.	1946 Dec. 31	By Premiums .. ..	£	s. d.
	„ Re-insurances ..	50,200	0 0		„ Salvages .. ..	103,000	0 0
	„ Charges .. ..	3,600	0 0		„ Re-insurance ..	4,800	0 0
	„ Balance .. ..	800	0 0		Recoveries .. ..	630	0 0
		54,694	0 0		„ Interest on Invest- ments .. ..	864	0 0
		£	109,294 0 0			£	109,294 0 0
1947. Dec. 31	To Claims .. ..	36,400	0 0	1947. Dec. 31	By Balance .. ..	54,694	0 0
	„ Re-insurances ..	1,200	0 0		„ Salvages .. ..	6,000	0 0
	„ Balance .. ..	23,514	0 0		„ Re-insurance ..		
					Recoveries .. ..	420	0 0
		£	61,114 0 0			£	61,114 0 0
1948 Dec. 31	To Claims .. ..	14,570	0 0	1948. Dec. 31	By Balance .. ..	23,514	0 0
	„ Re-insurances ..	240	0 0		„ Salvages .. ..	924	0 0
	„ Balance—being Profit .. ..	9,940	0 0		„ Re-insurance ..		
					Recoveries .. ..	312	0 0
		£	24,750 0 0			£	24,750 0 0

<i>Dr.</i>		SYNDICATE APPROPRIATION ACCOUNT.				<i>Cr.</i>	
1948. Dec. 31	To X Commission— 10% of £9,640 ..	£	s. d.	1948. Dec. 31	By Profit .. ..	£	s. d.
	„ N.D.C. .. ..	964	0 0			9,940	0 0
	„ Profit .. ..	300	0 0				
		8,676	0 0				
		£	9,940 0 0			£	9,940 0 0

## X AND OTHERS.

## ADJUSTED ACCOUNTS ALLOCATING PROFIT BETWEEN THE MEMBERS OF THE SYNDICATE

	£	s. d.	£	s. d.
To Net Profit for the year 1946, ended 1948 .. ..			8,676	0 0
Add Agent's Salary .. ..	800	0 0		
Ditto Commission .. ..	964	0 0		
			1,764	0 0
Amount divisible proportionately between Names ..			£10,440	0 0
X.— $\frac{1}{2}$ of £10,440 .. ..	3,480	0 0		
Less Agent's Salary .. ..	200	0 0		
	3,280	0 0		
Less Agent's Commission—10% of £3,280 .. ..	328	0 0		
			2,952	0 0
A.—Ditto .. ..			2,952	0 0
B.— $\frac{1}{2}$ of £10,440 .. ..	1,740	0 0		
Less Agent's Salary .. ..	200	0 0		
	1,540	0 0		
Less Agent's Commission—10% of £1,540 .. ..	154	0 0		
			1,386	0 0
C.—Ditto .. ..			1,386	0 0
Net Profit as per Accounts correctly allocated .. ..			£8,676	0 0

The interest on investments as per accounts was as follows :—

For the year 1946, closed 1948	..	..	£
			864

This interest on investments is divisible as follows :—

X. $\frac{1}{4}$ of £864	..	..	..	..	..	£
A. $\frac{1}{4}$ "	..	..	..	..	..	288
B. $\frac{1}{4}$ "	..	..	..	..	..	288
C. $\frac{1}{4}$ "	..	..	..	..	..	144
						144
						<u>£864</u>

The syndicate's adjusted profits for Income Tax are as follows :—

Net Profit, 1946 (closed 1948)	..	..	..	..	£	s.	d.
Less Interest on Investments	..	..	..	..	8,676	0	0
					864	0	0
Amount upon which Tax is still payable by members of the Syndicate by assessment in 1947/48	..				<u>£7,812</u>	<u>0</u>	<u>0</u>

This amount is divisible between the members as follows :—

X—Profit <i>re</i> Account of year 1946	..	..	£2,952	£
Less Share of Interest on Investments	..	..	288	
				<u>2,664</u>
A.—Ditto	..	..	..	2,664
B.—Profit, year 1946	..	..	1,386	
Less Share of Interest on Investments	..	..	144	
				<u>1,242</u>
C.—Ditto	..	..	..	1,242
Syndicate's Adjusted Profit correctly allocated	..	..		<u>£7,812</u>

The profit of an underwriting agent is a profit of the year in which the work is done, even though the amount cannot be fully calculated until two years later, when the account is closed; it is assessable to Profits Tax for the year in which the work is done (*Gardner, Mountain & D'ambrumeril v. C.I.R.* (1946), T.R. 149).

## CHAPTER VII.

## LOSSES.

**§ 1.—Setting off Losses in one Trade against Profits made in another—Rule 13.**

Under Rule 13 of Cases I and II, Sch. D, as amended by § 20, 1941, a person carrying on, either alone or in partnership with others, two or more distinct businesses chargeable under Case I or Case II is entitled, in arriving at the assessment for any year, to set off a loss made in one business against a profit made in another business.

The "loss" is the loss as adjusted for Income Tax purposes, just as the "profit" is the adjusted profit. The set-off is made in the assessment, *i.e.*, a loss made in the year forming the basis of assessment in the one business is set against the profit made in the year forming the basis of assessment in the other business. The relief is therefore normally given in the year of assessment immediately following that in which the loss was incurred.

Whether there are distinct businesses or merely departments of the same business to be assessed together, is a question of fact. The set-off takes place before deducting the wear and tear allowance. Unless previously settled with the Inspector when agreeing the adjustments of the respective accounts, the claim is made by way of notice of appeal against the assessment on the business showing a profit. It is thought also that such a claim could be made under the "error or mistake" provision (§ 24—1923).

The following illustration shows the practical value of the section to the taxpayer:—

**Illustration (1).**

X, a married man, carries on business as a grocer, and his adjusted profits for the year ended 30th June, 1946, as agreed with the Inspector of Taxes, amounted to £1,410.

He also carries on business as a hosier, and sustains a loss in the year ended 31st December, 1946, amounting to £1,290. This figure is also agreed with the Inspector of Taxes.

X's only other source of income is that from investments which bring him in an annual gross income of £230.

He desires to claim allowances and deductions, taking advantage of Rule 13 of Cases I and II, Schedule D.

**INCOME TAX COMPUTATION, 1947-48.**

	£	s.	d.	£	s.	d.
Business Profit—						
Grocer .. .. .	1,410	0	0			
<i>Less</i> Business Loss—						
Hosier .. .. .	1,290	0	0			
				120	0	0
<i>Deduct—</i>						
Earned Income Allowance						
$\frac{1}{3}$ th of £120 ..	20	0	0			
Personal Allowance (part)	100	0	0			
				120	0	0

He can therefore reclaim tax on his other allowances against investment income :—

Personal Allowance (Balance)	£80 at 9/-	£36	0	0
Reduced Rate Allowance	50 at 6/-	15	0	0
	75 at 3/-	11	5	0
Reclaim .. .. .		£62	5	0

If X were not entitled to set off the loss sustained in the hosiery business against the profit made in the grocery business, he would be liable to pay tax amounting to £421 10s. 0d. in addition to the £103 10s. 0d. suffered by deduction, thus :

Assessment—Grocer .. .. .	£1,410
Hosier .. .. .	Nil.
	1,410
<i>Deduct—</i>	
Earned Income Allowance ..	£235
Personal Allowance .. .. .	180
	415
Taxable Income .. .. .	£995

Chargeable—£50 at 3/- .. ..	£7 10 0
75 at 6/- .. ..	22 10 0
870 at 9/- .. ..	391 10 0
<b>Tax payable under Case I .. ..</b>	<b><u>£421 10 0</u></b>

Where one business is carried on by the husband and another by the wife, a loss on the business carried on by the one may be set off under Rule 13 against the profit on the business carried on by the other.

A partner can apply under Rule 13 his share of the firm's profit or loss for the year against any other business carried on by him, or against his share in the loss or profit of another firm in which he is a partner.

In arriving at a loss for the purposes of Rule 13, a life assurance or a capital redemption insurance business must leave in credit its investment income (R. 15, Cases I and II; § 27—1938).

In the case of a new business, the loss in one trade may form the basis for relief under Rule 13 for three years, since the loss for this purpose must be computed as a profit would be computed.

### Illustration (2).

A new company was formed to acquire two existing businesses. One business, A, was taken over on 1st July, 1945. The accounts of this business were made up to 31st January, 1947, showing a loss of £9,500. The other business, B, was taken over on 1st February, 1946, and made up its accounts to 31st January, 1947, disclosing a profit of £2,400. Show the assessments for the years 1945-46, 1946-47 and 1947-48, claiming relief under Rule 13.

Computing the loss of business A in the same manner as profits would be computed, the "losses" for Rule 13 purposes are as follows:—

1945-46. Actual $\frac{9}{12}$ ths of £9,500 .. ..	= £4,500
1946-47. First twelve months' trading $\frac{1}{12}$ ths of £9,500 .. ..	= £6,000
1947-48. Preceding year, $\frac{1}{12}$ ths of £9,500 ..	= £6,000

The assessments on business B are as follows :—

1945-46.	Actual $\frac{2}{3}$ ths of £2,400	..	=	£400	
	Less Set-off, Rule 13	..	..	400	Nil.
1946-47.	First twelve months' trading	..	£2,400		
	Less Set-off, Rule 13	..	2,400		Nil.
1947-48.	Preceding year..	..	£2,400		
	Less Set-off, Rule 13	..	2,400		Nil.

The balance of loss is available for relief under Section 33, 1926 (*see post*), viz.—

Loss	..	..	..	..	..	£9,500
Less Relieved	1945-46	..	..	..	£400	
	1946-47	..	..	..	2,400	
	1947-48	..	..	..	2,400	
						5,200
Carried forward	..	..	..	..		<u>£4,300</u>

It will be observed that had the profit on business B amounted to say £9,000, the assessments would have been £1,500, £9,000 and £9,000 respectively, against which would have been set off £1,500, £6,000 and £6,000, a total of £13,500 although the loss was only £9,500.

A similar position may arise where one business is a continuing one, and a new business is commenced with a loss.

## § 2.—Claims under § 34, Income Tax Act, 1918, and § 33, Finance Act, 1926.

Section 34 (as amended by § 30 (3)—1923) affords relief to a person who, in carrying on a trade, profession or vocation, or in the occupation of lands for the purpose of husbandry only, or in the occupation of woodlands assessed under Schedule D, sustains an adjusted loss during the year of assessment.

It enables a person who has sustained a loss in business to RECOVER, IN THE YEAR IN WHICH THE LOSS



IS INCURRED, an amount equal to the tax thereon, not exceeding the total tax borne on his statutory total income.

Notice of a claim under Section 34 must be given in writing to the Inspector of Taxes within one year after the end of the year of assessment for which the claim is made.

Where repayment has been made to a person for any year under Section 34, he is not entitled, in computing the amount of the assessment for any subsequent year, to a deduction of any portion of the amount in respect of which such repayment has been obtained.

By § 33, 1926, where a person sustains a loss in respect of which relief has not been wholly given under § 34, or under Rule 13 of Cases I and II or any other provision of the Income Tax Acts, he can claim that any LOSS NOT UTILISED MAY BE CARRIED FORWARD and set off against the next assessment on the same business for the SIX FOLLOWING YEARS. Any loss in respect of which relief is given under this section cannot be claimed under any other provision.

Relief under § 33, 1926, is to be given against the first available assessments in the succeeding six years (but the war years 1939-40 to 1945-46 inclusive are not counted as part of the six years; see below).

Where a loss is sustained, a person occupying woodlands who has elected, under Rule 7 of Sch. B, to be assessed under Sch. D, is entitled to relief under § 33, 1926, as though a trade were being carried on.

It should be noted that § 33, 1926, gives relief by reducing the next following assessment(s) *on the same business* only, whereas a claim under § 34 must, if made, be used against the *statutory* total income for the year of assessment in which the loss is sustained,

*i.e.*, where the loss exceeds in amount the statutory total income from all sources (not merely the income from the business), a refund of tax under § 34 can only be claimed of the tax paid, the excess of the loss over the statutory total income being carried forward under § 33, 1926.

(Under § 33 it will be noted that normally only *five* assessments are available for reduction by a loss brought forward, since, although the loss can be carried forward for *six* years, the first of such years has a *nil* assessment in any case (*see Harling v. Celynen Collieries' Workmen's Institute* (1940), T.R. 409). The loss for § 34 purposes is arrived at by adjusting the accounts in the usual way.)

There is an important exception, however, in the cases of a life assurance business (§ 13—1937), and capital redemption insurance business (§ 27—1938), for which a claim under § 34 can only be made in respect of a *trading loss*, *i.e.*, there must be a loss on the business as a whole; taxed interest and dividends cannot be deducted so as to convert what would otherwise have been a profit into a loss for a § 34 claim. Any income derived from the investments of the life assurance fund must be treated as profits of the business (Sch. D, Cases I and II, R. 15).

If, however, the result of trading is a loss prior to writing back such taxed interest and dividends as formed part of the trading receipts, the Commissioners grant a refund of tax on the trading loss only, leaving the balance of the adjusted loss to be carried forward.

The time limit for carrying forward losses under § 33, 1926, is extended when any of the six years for which a loss could be carried forward includes any of the years 1939-40 to 1945-46 (inclusive), by such of those years as is subsequent to the loss (§ 22—(No. 2) 1945). In respect of a loss in 1933-34 or any later year up to and including 1938-39, seven years are added, making the period 13 years. In the case of a loss in the war years, the six year period will start from 6th April, 1946.

**Illustration (1).**

Loss in year to	Normal last year of assessment for relief	Amended last year for relief
31/12/34	1940-41	1947-48
31/3/37	1942-43	1949-50
30/6/39	1945-46	1951-52
31/12/45	1951-52	1951-52*

\*No amendment, as none of the years following the loss is a relevant year.

It should be noted that losses under § 19, 1928 (see *post*) are included in losses under § 33 and the above extension applies. The effect on § 19, 1932 (see *post*) will be obvious.

Where in 1945-46 or any later year of assessment, a loss brought forward exceeds the Case I assessment on the business, the balance of the loss may be set against any interest or dividends on investments arising in that year of assessment, provided such interest or dividends would be trading receipts but for the fact that they are taxed under some other provision (§ 22—(No. 2) 1945), *i.e.*, they must be income of the business in which the loss was sustained.

It must be noted that this relief is limited to Case I, and in the case of life assurance or capital redemption, the loss is to be computed as for Rule 15, Rules of Cases I and II, *i.e.*, investment income is included in the accounts in deciding the amount of the loss. Appeal can be made in the usual way where a dispute arises.

**Illustration (2).**

Company's Assessment 1947-48	..	..	£1,000
Less Loss brought forward	..	..	1,150
Balance of loss	..	..	<u>£150</u>
Investment Income 1947-48	..	..	£200
Less Balance of loss	..	..	150
Balance of income	..	..	<u>£50</u>

			£	s.	d.
Tax paid, £200 at 9/-	..	..	90	0	0
Tax repayable, £150 at 9/-	..	..	67	10	0
Tax borne .. ..			<u>£22 10 0</u>		

\*i.e., Tax on £50 at 9/-

The loss to be taken is, legally, that of the year to 5th April (found by splitting accounts where necessary), but the Revenue will allow the accounting year to be treated as co-terminous with the fiscal year, although not in the first three years of a business (four if "actual" is claimed for the second and third years' basis), nor in the last year. Moreover, the accounting year concession will not be allowed in a year following a claim based on a loss for a year to 5th April, or where accounts are made up for irregular periods.

In the application of § 33, 1926, to a partnership, the amount of profits or gains against which any partner's share of the loss sustained by the firm may be carried forward, must be taken to mean such portion of the partnership Schedule D assessment for any year as the partner in question would be required to include in his return of total income for that year (§ 33 (2)—1926). It follows, therefore, that should a partner die or retire from the firm before full relief had been given for his share of the loss, the balance thereof could no longer be carried forward by the firm.

### Illustration (3).

A and B are in partnership, sharing profits in the proportions of 3 : 2 after receiving salaries and interest on capital as under :—

Salaries			Interest on Capital		
A .. ..	£500	A .. ..	£200		
B .. ..	£400	B .. ..	£100		

Accounts were prepared to 5th April in each year and adjusted results were :—

Year ended 5th April, 1945	..	Profit	£2,000
„ „ 5th April, 1946	..	Loss	3,600
„ „ 5th April, 1947	..	Profit	400
„ „ 5th April, 1948	..	Profit	1,500

Neither partner had any other income. Section 34 claims were made by both partners in respect of the loss, the balance of which was carried forward under Section 33. B died on 5th April, 1948, after which A carried on the business alone. No claim was made under Rule 11 for the business to be treated as discontinued and newly commenced on B's death.

Assessments.		Firm.		Allocation.	
				A	B
		£		£	£
1945-46 Profits of year ended 5/4/45.	..	2,000	Salary ..	500	400
			Interest ..	200	100
			Balance 3 : 2	480	320
				<hr/>	<hr/>
				1,180	820
Less Relieved under § 34	2,000			1,180	820
		<u>Nil</u>		<u>Nil</u>	<u>Nil</u>
1946-47 Profits of year ended 5/4/46.	..	<u>Nil</u>		<u>Nil</u>	<u>Nil</u>
1947-48 Profits of year ended 5/4/47.	..	400	Salary ..	500	400
			Interest ..	200	100
				<hr/>	<hr/>
				700	500
			Less Balance 3 : 2	480	320
				<hr/>	<hr/>
				220	180
Less loss brought forward under § 33	400			220	180
		<u>Nil</u>		<u>Nil</u>	<u>Nil</u>
1948-49 Profit of year ended 5/4/48	..			1,500	—
Less Balance of loss brought forward attributable to A	.. ..			780	—
				<hr/>	<hr/>
Assessment .. .. .				<u>£720</u>	

The loss is allocated to the partners as under :—

	Firm	A	B
	£	£	£
Adjusted loss .. .. .	3,600		
<i>Add salaries and interest</i> ..	1,200	<i>Cr.</i> 700	500
“ Balance ” 3 : 2 .. .. .	4,800	<i>Dr.</i> 2,880	1,920
<i>Less salaries and interest</i> ..	1,200		
	3,600	2,180	1,420
Relief given under Sec. 34 1945-46	2,000	1,180	820
Loss carried forward .. .. .	1,600	1,000	600
Relieved under § 33—			
1947-48 .. .. . £400		£220	180
1948-49 .. .. . 780		780	
	1,180	1,000	
Balance unrelieved .. .. .	<u>£420</u>	<u>£ —</u>	<u>£420</u>

The balance of £420 attributable to B, cannot be carried forward beyond 1947-48, since B ceased to be a partner of the firm in that year.

The Inland Revenue take the viewpoint that the loss in respect of which a § 34 claim is made is a loss of earned income, and therefore insist that it be set off against earned income first, thus restricting the earned income allowance. The only exceptions are :—

(1) Where a firm makes a loss, the claim by a *sleeping* partner will be set off first against his share of the firm's assessment (which to him is unearned), and his other unearned income ; and

(2) Where the wife has earned income, a claim by the husband will be set against his income from all sources before reducing the wife's earned income. Similarly, where the wife makes a business loss, her income must be absorbed first.

This interpretation is often resisted and taken to appeal, and some bodies of General Commissioners decide against the Revenue, allowing set-off against unearned income first. The Special Commissioners uphold the Revenue view. In the illustrations given in this book, the Revenue practice is followed, but readers should bear the above remarks in mind.

The following illustrations exemplify the application of § 34 claims in various circumstances.

**Illustration (4).**

A farmer had the following income for 1947-48 :—

Farm, assessed under Schedule B, £300.

Directors' Fees, £480.

Interest on  $3\frac{1}{2}\%$  War Loan £520.

Dividends free of tax £440.

For the year ended 31st March, 1948, he paid bank interest of £100 on overdraft employed on the farm and he had reclaimed tax under § 36, 1918, in respect thereof. His accounts for that year showed an adjusted loss of £800, after charging the bank interest, and he made claims under Rule 6, Schedule B, and § 34. He is a married man, with four children, of whom two are over 16, one of the latter being still at school.

COMPUTATIONS, 1947-48.

			Original.	For § 34 claim (Rule 6). Nil.
Schedule B	..	..	£300	
Schedule E	..	..	480	£480
Schedule D, Case III	..	..	520	520
Dividends	..	..	800	800
			<hr/>	<hr/>
			2,100	1,800
Less Bank Interest	..	..	100	
Loss	..	..		800
			<hr/>	<hr/>
			2,000	1,000
<i>Deduct Allowances—</i>				
Earned Income $\frac{1}{3}$ th of £780	£130			Nil.
Personal	..	..	180	£180
Three Children	..	..	180	180
			<hr/>	<hr/>
			490	360
			<hr/>	<hr/>
Taxable Income	..		<u>£1,510</u>	<u>£640</u>

Chargeable at 3/-	£50	£7 10 0	£50	£7 10 0
at 6/-	75	22 10 0	75	22 10 0
at 9/-	1,385	623 5 0	515	231 15 0
				<hr/>
				261 15 0
Tax paid ..		£653 5 0		653 5 0
				<hr/>
Tax Repayable ..				£391 10 0
				<hr/>

The claim may be computed :—

Cancellation of Schedule B assess-

ment under Rule 6 .. .. £300

Less Earned Income Allowance 50

---

£250 at 9/- £112 10 0

Cancellation of Schedule E assess-

ment .. .. £480

Less Earned Income Allowance 80

---

400

Balance of loss £(800—480) .. 320

---

£720 at 9/- 324 0 0

---

436 10 0

Less Cancellation of repayment under § 36 as

interest is debited in the farm Accounts in

arriving at the loss, £100 at 9/- .. .. 45 0 0

---

£391 10 0

If the claim were agreed in time, the second instalment under Sch. B would be discharged, and the repayment reduced *pro tanto*.

The small farmer assessed under Sch. B has an advantage under § 34 as compared with persons assessed under Sch. D since he claims *first* relief under Rule 6, thus cancelling the Sch. B assessment, whereas, in the case of a person assessed under Sch. D, the original assessment stands ; the net result is that the small farmer saves the tax on the amount of the assessment as well as being repaid on the loss under § 34 against other income, whereas the others are only repaid under § 34.



**Illustration (5).**

A B and C are in partnership sharing profits and losses equally, after charging salaries and interest on capital, amounting to—A, £600; B, £800; C, £400.

For the year ended 31st December, 1946, the adjusted profits were £300; for 1947 the adjusted loss was £240.

1947-48, assessment £300.

Divided among partners :—

		A.	B.	C.
£		£	£	£
1,800	Salaries and Interest ..	600	800	400
1,500	"Loss," to be divided in profit sharing ratio	500	500	500
<u>£300</u>		<u>£100</u>	<u>£300</u>	<u>Loss £100</u>

Although the result of the division is as shown, the firm can only be assessed on £300, which is shared by A and B in the ratio of 100 : 300; *i.e.*, A, £75, B, £225. C can claim no relief on his share although from his point of view it is a loss. Although the claims under both § 34 and § 33, 1926, are personal and individual claims to be made by each partner separately, no claim for relief in respect of a loss can be made by any partner where the *firm* has an adjusted profit, since the firm is the unit of assessment.\*

For the purpose of arriving at the amounts of loss on which the individual partners may claim relief, the loss of £240 is divided—

		A.	B.	C.
£		£	£	£
1,800	Salaries and Interest	600	800	400
240	Adjusted Loss			
<u>£2,040</u>	Balance .. ..	680	680	680
1,800				
<u>£240</u>	<i>Loss</i>	<u>£80</u>	<u>£120</u>	<u>Loss £280</u>

\* Although the above is the Revenue practice, and is reasonable, it is understood that some bodies of Commissioners, including the Special Commissioners, have given relief under § 34—not § 33—to an individual partner on his "loss" although the firm has made a profit, or the firm's loss is less than his share, despite the fact that other partners may escape tax on some or all of their shares of profit.

Since the *firm* has made a loss of £240, B's share for tax purposes is nil, and A and C share the adjusted loss of £240, in the ratio, 80 : 280 ; i.e., A  $\frac{80}{360}$  of £240 = £53, and C  $\frac{280}{360}$  of £240 = £187. A can therefore claim under § 34 on £53 and C on £187, or either (or both) may elect to allow the loss to be carried forward under § 33, 1926, *against their respective shares* of the next Sch. D assessment on the firm.

The claim under § 34 must be made by reference to the taxpayer's Statutory Total Income from all sources, and automatically reduces such total income. In the case of an individual, this may make it inadvisable to claim the relief, as the allowances may be sufficient to absorb, or substantially absorb, the total income, and by making the claim the allowances would be lost. Each case must be worked out to see if the claim is worth making, having regard to the expectation of alterations in the rate of tax, the effect on Sur-tax, etc.

It should be noted that all claims under § 34 are to be determined by the Special or General Commissioners, against whose decision there is no appeal, since the application for relief is not an appeal against an assessment (*Bruce v. Burton*, (1901), 4 T.C. 399).

A loss incurred in the first year of a business will normally enter into the computation of the assessments for several fiscal years. To the extent that it is used to offset a profit in any year, relief has been effectively allowed for the purposes of § 33, 1926, and such portion cannot be carried forward ; nor can a notional loss be carried forward (*C.I.R. v. Scott Adamson* (1932), 17 T.C. 679).

#### Illustration (6).

A commenced business on 1st January, 1942, and discontinued on 30th September, 1947. The adjusted profits and losses were as follows :—

Year ended 31st December, 1942	Loss	£1,400
do. 1943	Profit	2,000
do. 1944	„	4,000
do. 1945	„	1,200
do. 1946	Loss	1,000
Period ended 30th September, 1947	„	100

A's wife had an earned income of £300 per annum. A owned the freehold house in which they lived, assessed at £100 (net). A did not claim under § 34 in respect of the loss in 1942, but made a claim in respect of the losses in the closing years.

YEAR.	ASSESSMENTS.	£
1941-42	Proportion of first accounts .. ..	Nil.
1942-43	Result of first 12 months .. ..	Nil.
1943-44	Previous year's results .. ..	Nil.
1944-45	do. .. ..	£2,000
	Less Loss brought forward ..	1,400
		<hr/> 600
1945-46	Previous year's results .. ..	4,000
1946-47	do. .. ..	1,200
	Less § 34 claim .. ..	1,000
		<hr/> 200
1947-48	" Actual " .. ..	Nil.

But a claim could be made under § 34 against the Schedule A assessment, on the loss incurred in the year of assessment, *i.e.*, from 6th April, 1947, to 30th September, 1947,  $\frac{5}{12}$ ths of £100 = £67.

#### Illustration (7).

S commenced business on 1st June, 1945. He made up his accounts to 31st March, 1946, showing an adjusted loss of £61. His accounts to 31st March, 1947, showed a profit of £144.

YEAR.	ASSESSMENT.	£	£
1945-46	Actual " profits " from 1st June, 1945— 5th April, 1946 .. ..		Nil.
1946-47	Result of first 12 months, 1st June, 1945 — 31st March, 1946, loss .. ..	61	
	2 months to 31st May, 1946, profit $\frac{1}{2}$ of £144 .. ..	24	
		<hr/>	Nil.
	£24 profit has been off-set against £24 of the £61 loss, leaving to carry for- ward only .. ..	37	
1947-48	Previous year's profits .. ..	144	
	Less loss as above .. ..	37	
		<hr/>	107

**Illustration (8).**

A commenced business on 1st May, 1954. His accounts to 31st December, 1945, showed a loss of £600. His accounts to 31st December, 1946, and 31st December, 1947, showed profits of £2,000 and £3,000 respectively.

YEAR.	ASSESSMENT.	£	£
1945-46	Actual "profits" from 1st May, 1945, to 5th April, 1946—		
	Loss to 31st December, 1945 ..	600	
	Profit to 5th April, 1946, $\frac{1}{2}$ ths of £2,000 .. .. .	500	
			Nil.
1946-47	Result of first 12 months' trading—		
	8 months to 31st Dec., 1945, loss	600	
	4 " " 30th April, 1946, $\frac{1}{2}$ ths of £2,000 profit ..	667	
			67
1947-48	Profits of year ended 31st Dec., 1946..		2,000

NOTE.—Relief for £500 loss was obtained in 1945-46, by set-off against £500 profits. Similarly, relief for £600 loss was obtained in 1946-47. Although this results in over-relief, the Inland Revenue have no redress, owing to the mandatory wording of the rules for arriving at the assessments of the first two years. No loss can, however, be carried forward.

**Illustration (9).**

If a claim under § 34, 1918, were made against other income in respect of the net loss of £100 for the period from 1st May, 1945, to 5th April, 1946 (Year 1945-46), in the previous example the effect on the future assessments would be as follows:—

Sub-section (4) of that section provides that where repayment has been made for any year under § 34, no portion of the amount in respect of which such repayment has been obtained can be deducted in computing the assessment for any subsequent year.

The assessment for the year 1946-47, would therefore be calculated as follows, viz:—

YEAR.	ASSESSMENT.	£	£
1946-47	Result of first 12 months' trading, viz:—		
	8 months to 31st December, 1945, loss	600	
	Less: Amount in respect of which repayment obtained under § 34.. ..	100	
	Loss	500	
	4 months to 30th April, 1946— $\frac{1}{2}$ ths of £2,000, profit .. ..	667	
			<u>£167</u>

*Concessional Allowances.*

Where wear and tear allowances have not been wholly used up in arriving at the assessment, a concession is given whereby the unused wear and tear allowance can be added to the loss for the purposes of a § 34 claim. The concession is that so much of the wear and tear allowance as cannot be used in the assessment of the year, but not exceeding the allowance for the year of assessment, may be added to the loss (or used to convert a profit into a loss). The amount of wear and tear allowance so used for § 34 cannot then be carried forward.

This concession recognises that the loss is understated to the extent that no depreciation has been charged, but takes into account the fact that it is not understated by more than one year's depreciation.

*Illustration (10).*

Profit for year ended 31st December, 1945 ..	£500
Loss „ „ „ „ „ 1946 ..	100
Wear and Tear Allowance, 1946-47 .. ..	680
do. brought forward ..	310
Other Income, Schedule A Net Annual Value ..	700
Schedule D, Case I Assessment, 1946-47 .. ..	£500
Less Wear and Tear Allowance—	
brought forward .. ..	£310
for year 1946-47 .. ..	680
	<hr/> 990
Unabsorbed Wear and Tear Allowance ..	<u>£490</u>
SECTION 34 CLAIM—	
Loss, 1946-47 .. ..	£100
Add Unabsorbed Wear and Tear Allowance .. ..	490
	<hr/>
AVAILABLE AGAINST OTHER INCOME	<u>£590</u>

The unabsorbed Wear and Tear Allowance has been used for the purposes of the concessional § 34 claim, and cannot be carried forward, but the Case I assessment in 1946-47 will be NIL. The net effect is that a repayment is given on the £490, instead of its being carried forward to reduce later assessments. Had the Schedule A assessment been £200 only, £100 of the unabsorbed Wear and Tear Allowance would be used for the concessional § 34 claim, leaving £390 to be carried forward *as* Wear and Tear Allowance.

### Illustration (11).

In the above illustration, had the Wear and Tear Allowance for 1946-47 been £310, and that brought forward, £680, the computation would have read :—

Sch. D, Case I assessment, 1946-47		
Profit of previous year ..		£500
Less Wear and Tear, 1946-47 ..	£310	
do. brought forward	680	
		<u>990</u>
Unabsorbed Wear and Tear allowance		<u>£490</u>

Of this, only the current year's allowance, £310 is available to be added to the loss for § 34 purposes, the balance of £180 being carried forward as wear and tear.

### Illustration (12).

Profit for year to 30th September, 1945 ..	£200
do. 1946 ..	50
Wear and Tear Allowance, 1946-47 ..	275
Case I Assessment, 1946-47 .. ..	£200
Less Wear and Tear Allowance, 1946-47	275
Unabsorbed Wear and Tear Allowance	<u>£75</u>

### SECTION 34 CLAIM, 1946-47—

Profit year ended 30th September, 1946 ..	£50
Deduct : Concessional Wear and Tear Allowance	75
Notional Loss .. ..	<u>£25</u>

Tax can be reclaimed under § 34 on £25 against other income. The assessment for 1947-48 will be £50 less the Wear and Tear Allowance for 1947-48, since the Wear and Tear Allowance for 1946-47 has been used under § 34.

The result of the concession is to give smaller ultimate relief.

In the case of partnerships, the concessional allowance will only be made if all the partners (not only those claiming under § 34) agree that the relief for wear and tear allowance so given shall be binding on the firm, and not only on those partners who have claimed under § 34, so that in the event of a subsequent change in the partnership the partners who have not claimed under § 34 shall be precluded from claiming further relief in respect of such wear and tear allowance.

A concession can be obtained whereby the operation of § 33, 1926, is expedited in those cases where by splitting accounts an actual loss for the fiscal year can be shown. This is best explained by illustration.

#### Illustration (13).

A's accounts were made up to 30th June, showing the following results :—

Year to 30th June, 1945.	Profit	..	..	£2,000
do. 1946.	Loss	..	..	£9,000
Assessment 1946-47	..	..	..	£2,000

The *actual* loss for the fiscal year 1945-46 is—

$$\frac{3}{12}\text{ths of } £2,000 - \frac{9}{12}\text{ths of } £9,000 = £6,250 \text{ loss.}$$

A had other income, which gave him a statutory total income for 1945-6 of £4,600. A § 34 claim on £4,600 would be allowed, leaving to carry forward under § 33, 1926—

$$£9,000 - £4,600 = £4,400 \text{ loss.}$$

This loss would normally fall to be deducted first against the assessment for 1948-49, since the assessment for 1947-48 (based on the loss) would be nil. By concession, however, it can be set first

against the assessment of 1946-47, leaving £4,400 - £2,000 = £2,400 to carry forward. The time limit is likewise accelerated, i.e., the balance of loss cannot be carried forward beyond 1951-52.

A curious position may arise where a business is discontinued, as will be seen from the following illustration.

#### Illustration (14).

A trader closed down his business on 31st December, 1946. His accounts as adjusted for Income Tax purposes disclosed the following results:—

Loss to 31st December, 1944	£500
" " " " 1945	£1,000
Profit " " " 1946	£4,000

He had a large income from dividends, and in 1944-45 and 1945-46, he reclaimed under § 34 on the losses of £500 and £1,000.

On the discontinuance of the business, the assessment for 1945-46 has to be increased to "actual," viz.,  $\frac{9}{12}$ ths of £1,000 loss +  $\frac{3}{12}$ ths of £4,000 profit = £250 profit.

The taxpayer has been repaid tax on the whole loss (against dividends); his income now includes £250 earned income, and according to the Revenue practice that should be off-set by the § 34 claim, thus depriving him of earned income allowance thereon.

Since, however, the decision of the Commissioners (Special or General) on a § 34 claim is final, the claim cannot be reopened. The result is that the taxpayer must be given the earned income allowance on the £250. Moreover, the Revenue cannot disallow the £750 of the loss which has been taken into account in arriving at the amended assessment, in spite of the fact that tax has been repaid thereon under § 34.

On the death of a husband, his widow may succeed to the business. Although legally the assessments should be made as if the business had been discontinued and a new one set up, it is common, for convenience, to continue the assessments on the preceding year basis. Losses prior to the death cannot be carried forward, however.



*Losses carried forward beyond the statutory limit.*

Wear and tear allowances must be deducted in assessments before deducting any loss brought forward under § 33, 1926, or § 19, 1928 (as to which see § 3 of this chapter). It may be, therefore, that at the expiration of six years (plus the "war" years, where appropriate) following the year in which a loss was incurred, relief for the loss has not been wholly obtained, owing to the fact that wear and tear allowances have absorbed the assessments which would otherwise have been available for relief in respect of the loss. This position is now met by § 19, 1932, if, at the end of the period for which a loss can be carried forward under § 33, 1926, or § 19, 1928, it can be shown that if wear and tear allowances had not been deducted first, relief would have been given for the whole or part of the balance of loss, then so much of the loss as has been displaced by wear and tear allowances can be carried forward beyond that period until it can be utilised. The net effect is therefore that a taxpayer can now utilise losses or wear and tear allowances to his best advantage. A deduction for wear and tear must not be utilised more than once under this section.

The relief does not extend to the set-off of a loss under § 29, 1927 (*i.e.*, losses utilised against income received from a company to which the taxpayer has transferred his business—see § 4 of this chapter).

Where there are losses available under § 33, 1926, or § 19, 1928, these must be deducted in priority to any loss under § 19, 1932. This means that future assessments are computed in the first place as if the § 19, 1932, loss did not exist, then the § 19, 1932, loss is deducted, thus ensuring that no time limit is placed on the latter.

## Illustration (15).

Year to Dec. 31st	Profits.	Losses.	Wear and Tear Allowance.
1944	£ 160	£	£
1945		600	1945-46 95
1946	100		1946-47 91
1947	220		1947-48 87
1948	370		1948-49 84
1949	110		1949-50 81
1950		200	1950-51 79
1951	430		1951-52 77
1952	500		1952-53 75
			1953-54 78

Year	Assessment.					Wear and Tear Allowance c/f.	Losses c/f.		Losses for § 19 (1932).	
	Previous Year's Profits.	Less Wear and Tear Allowance.	Amount	Less Loss b/f.	Net.		Amount	Last Year to which available	Potential.	Actual.
1945-46	£ 160	£ 95	£	£	£	£	£		£	£
1946-47	—	—	—	—	—	91	600	1951-52		
1947-48	100	87 + 13	—	—	—	13			100	
1948-49	220	84 + 78	58	58	—	78 78	58	do.	162	
							542			
1949-50	370	81	289	289	—		289	do.	81	
							253			
1950-51	110	79	31	31	—		31		79	
							222*		422	222
1951-52	—	—	—	—	—	77	200	1956-57		
1952-53	430	75 + 77	278	200	78	77	200†			
				Less § 19 (1932) Loss	78 nil					- 78 144 -144
1953-54	500	78	422	† 144	£278					

\* This loss, incurred in the year 1945-46 cannot be carried forward under § 33, 1926, beyond the year 1951-52, but, under § 19, 1932, so much thereof as could have been utilised but for the deduction of Wear and Tear Allowances, may continue to be carried forward.

The amount utilised in Wear and Tear Allowances is £422 (see "Potential" column), but as the actual unutilised loss is only £222, this amount may continue to be carried forward. Had, say, £500 been unutilised, only £422 could be carried forward.

† The loss in 1950-51 must be utilised within the following 6 years before relief is given in respect of the substituted loss under § 19, 1932.

‡ Under § 19, 1932.

In general terms, the same result would be obtained if losses were deducted in priority to wear and tear allowances, but the Acts require the reverse procedure to ensure that no over-allowance is given, e.g., if the business were sold to a company and relief were claimable under § 29, 1927.

**§ 3.—Annual charges carried forward as a  
“loss” (General Rule 21, and § 19,  
Finance Act, 1928).**

Where an assessment has been made under General Rule 21 in respect of a payment made wholly and exclusively for the purposes of the business, the amount on which tax has been paid under that assessment will, for the purposes of § 33, 1926, be treated as though it were a loss sustained in that business. It can therefore be carried forward for the six years following the year of assessment for which the General Rule 21 assessment was made (plus the “war years” where appropriate, as for § 33). Rule 21 assessments on copyright royalties are excluded, as such royalties are allowed as deductions in the accounts. No relief will be allowed under this section in respect of any such payment or any part of any such payment which is not ultimately borne by the person assessed or which is charged to capital (§ 19—1928).

The justice of this relief will be seen when it is remembered that in any year in which a person has insufficient income taxed at source or by assessment to cover the annual charges from which tax is deductible, he is required to pay over the tax on the excess of such charges over his taxable profits under General Rule 21.

Any payment from which tax is deductible at source is disallowed as an expense in the accounts, because, being entitled to deduct tax from the payee, the payer cannot expect to reduce his income by the payment, and thus reduce the tax payable to the Revenue. He must pay tax on his income before deducting the annual payment.

In the case of a General Rule 21 assessment, however, the tax deducted is not retained by the payer of the annual charge, but paid over to the Revenue in addition to the tax on his income, and it would therefore be equitable to allow the charge as a business expense. The charge is still disallowed, however, but § 19, 1928, gives relief by allowing it to be treated as a loss. If relief were not so given, there would be an over-assessment in the amount of the General Rule 21 assessment, taking a period of years into account.

### Illustration.

A limited company made the following profits :—

Year ended 31st March, 1943	..	£2,000
do. 1944	..	100
do. 1945	..	520
do. 1946	..	4,000

The company also had an income from taxed sources of £200 per annum, and paid debenture interest of £700 per annum. This interest has, of course, been “ added back ” in arriving at the above profits.

The assessments on the company would be as follows :—

1943-44—£2,000—which is sufficient to cover the debenture interest, from which tax is therefore deducted under General Rule 19, and retained by the company.

1944-45—£100—The profits “ brought into charge to tax ” in this year are thus £100 plus the taxed income of £200, a total of £300. To that extent tax is deducted from debenture interest under Rule 19, but the tax deducted from the remaining £400 of debenture interest is under Rule 21. An assessment (in addition to the Case I assessment of £100) will therefore be raised on this £400, which can then be carried forward as a loss (§ 19—1928).

1945-46—£520, less “ loss ” brought forward £400 = £120. Similar remarks to those relating to 1941-42 apply, and £380 will be assessed under Rule 21 and carried forward as a “ loss.”

1946-47—£4,000, less "loss" brought forward £380 = £3,620.

"This assessment is sufficient to cover the debenture interest, from which tax is therefore deducted and retained by the company under General Rule 19.

Comparing "like with like," it will be seen that the position over four years is as follows:—

Year to March 31st.	Profits.	Debenture Interest Paid.	Real Profit or Loss.		Income charged to Tax.			Tax is recouped from Debenture Interest on.	Therefore tax is borne on.
					Case I.	Other Income.	Rule 21.		
	£	£	£		£	£	£	£	£
1943 ..	2,000	700	P. 1,300	1943/44.	2,000	200	—	700	1,500
1944 ..	100	700	L. 600	1944/45.	100	200	400	700	—
1945 ..	520	700	L. 180	1945/46.	120	200	380	700	—
1946 ..	4,000	700	P. 3,300	1946/47.	3,620	200	—	700	3,120
	<u>£6,620</u>	<u>£2,800</u>	<u>£3,820</u>		<u>£5,840</u>	<u>£800</u>	<u>£780</u>	<u>£2,800</u>	<u>£4,620</u>

The real income is £3,820 + £800 of taxed income = £4,620, which is the net amount on which tax is borne as shown by the last column. Had the Rule 21 assessments not been allowed as "losses," an over-payment on £780 would have resulted.

It will be observed that § 19, 1928, does not extend to cases in which interest is charged to capital, *e.g.*, it would not cover interest paid on construction capital under § 54, Companies Act, 1929, or to interest on loan capital similarly employed, since in both cases the interest in question is specifically excluded from being at any time a charge upon the profits of the company.

#### § 4.—Business transferred to a Limited Company.

Owing to the succession rules (*see* Chap. IV, § 10), when a business is sold by a sole trader or partnership to a limited company, it must be assessed as if it were discontinued and recommenced on the date of transfer. As a result, if a loss were incurred prior to the transfer, no relief would be available under § 33, 1926, in assessments on the company subsequent to the transfer.

Where the members of the company are the same persons as the sole trader or partners who were engaged in the former business this would entail a hardship, since there has been merely a technical change in the ownership of the business.

It is true that the legal owner of the business is now the company, but since the former owners are the proprietors of the company, they are still the persons beneficially interested.

Section 29, 1927, meets the position by providing that any former proprietor of the business is entitled to relief for losses incurred prior to the transfer of the business, subject to the following conditions:—

(1) The business was transferred to the company in consideration solely or mainly of an allotment of shares of the company to the vendor(s) who previously carried on the business, or to his or their nominee(s).

(2) He must be the beneficial owner of the shares allotted to him or his nominees, throughout the year of assessment for which relief is claimed (in the first year from the date of transfer to the following 5th April).

(3) The company must have carried on the business throughout the year of assessment for which relief is claimed (in the case of the first year, from the date of transfer to 5th April).

Any loss which the individual could have carried forward under § 33, 1926, or § 19, 1928, (as extended for "war losses" by § 22—(No. 2) 1945) can then be carried forward and set off against any income derived by him from the company, whether as dividends on the shares or otherwise. The loss must be deducted or set off in the first place against that part, if any, of the income in respect of which he has been or is liable to be assessed to tax for that year, then against

income taxed by deduction. Relief in respect of the latter must be claimed by giving notice in writing to the Inspector of Taxes not later than twelve months after the end of the year of assessment to which the claim relates. The appropriate repayment will then be made.

The loss is set against the transferor's earned income from the company before applying it to unearned income. This is reasonable—as had the business been continued without transfer, the loss would have been set against future profits which would be earned income.

It should be noted that in this case, as in the case of all other loss claims, a partner can claim relief in respect of his share of the firm's loss.

#### Illustration.

A and B carried on business in partnership until 31st May, 1945, when they transferred their business to A B Ltd., being allotted shares as consideration for the transfer. A and B shared profits equally.

The adjusted profits and losses were as follows :—

A and B

Year ended 30th September, 1942	Profit	..	£8,000
do.	1943	Loss	.. 5,000
do.	1944	Profit	.. 2,000

A B Ltd.

Year ended 30th September, 1945	Profit	..	£1,700
do.	1946	„	.. 1,300

Directors' Fees were paid as follows :—

Four months ended 30th September, 1945, £400 each.

Year                    „                    „                    1946, 1,200 „

Dividend paid 1945, £500 each.

A made a § 34 claim in 1943-44.

## ASSESSMENTS—

Year.	A's share.	B's share.	Total Assessment on Firm.
1943-44	£4,000. A claims under § 34 on £2,500.	£4,000.	£8,000.

1944-45	Nil. Increased under § 31, 1926, to penultimate year, viz. :— £1,125.	Nil. £1,125.	Nil. $\frac{6}{12}$ of £2,000 + $\frac{6}{8}$ of £1,667* = £2,250.
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B's assessment is reduced by loss brought forward to *nil*, reducing firm's assessment to £1,125, to be borne by A; B has £1,375 loss to carry forward.

\*See below.

1945-46 The profit for the year ended 30th September, 1945, is apportioned between the firm and the company as follows :—

Profits per accounts .. .. .	£1,700
Add Directors' Fees wholly chargeable to company .. .. .	800
	<u>£2,500</u>
Firm's proportion—8 months ..	£1,667
Company's proportion—4 months	£833
Less Directors' Fees .. .. .	800
	<u>33</u>
	<u>£1,700</u>

Firm's assessment (6th April to 31st May, 1945).

$$\frac{1\frac{5}{8}}{8} \times £1,667 = £382.$$

A's proportion .. £191

B's „ .. £191

Less Loss b/f .. 1,375

= *nil* reducing firm's assessment to £191 to be borne by A.

Leaving to c/f .. £1,184



Directors' fees :—

A, £400 + $\frac{6}{12}$ of £1,200 =	<u>£1,000</u>	
B, do.	1,000	
Less Loss b/f ..	1,184	Nil.
Leaving balance ..	<u>£184</u>	

to claim as set off against dividend, reclaiming the appropriate tax overpaid.

It should be noted that any Wear and Tear allowances to which effect has not been given in the vendor's assessments cannot be carried forward to the company.

The company's assessments would be—

1945-46—£33 + $\frac{6}{12}$ ths of £1,300	=	£683
1946-47—£33 + $\frac{6}{12}$ ths of £1,300	=	£900
1947-48—Decided upon by Commissioners of Inland Revenue under § 34,		
1926—probably .. ..		£1,300

Subject to any claim arising for adjustment of the assessments for 1946-47 and 1947-48 to the actual profits of those years.

### § 5.—Losses incurred in transactions assessable under Case VI (§ 27—1927).

Where in any year of assessment a person is assessed in respect of any profits or gains under Case VI, Schedule D, any loss incurred in respect of any transaction which, had it shown a profit would have been assessable under Case VI, may be set off against the profits in respect of which he is assessed under Case VI in that year. Any balance of such loss may be carried forward and set off against the next Case VI assessment(s), subject to a six years' time limit.

It should be noted that the set-off is against *any* Case VI assessment, and is not limited to future assessments on the same source. This is the only relief that can be claimed in respect of a "Case VI

loss ”; § 34 does not apply. In the case of a partner, as is usual, his share of any profit or loss must be taken for the purposes of the claim.

**Illustration.**

A, during the year 1947-48, incurred a loss of £1,000 on an underwriting speculation. In the same year he made a profit of £400 from letting furnished rooms. Under § 27, 1927, the loss will be set-off against the profit, extinguishing the assessment, and the balance of £600 can be carried forward and set against the next Case VI assessment on any annual gain.

Had there been no profit of any kind assessable under Case VI in 1947-48, then the whole £1,000 loss could be carried forward.

## CHAPTER VIII.

## SUR-TAX.

## § 1.—The Basis of Sur-Tax.

Sur-tax is an additional Income Tax charged on the statutory total income of an individual where it exceeds £2,000. The charge is at graduated rates (§ 38—1927). Sur-tax is payable as a deferred instalment of Income Tax on the 1st January following the end of the year of assessment (§ 42—1927), *i.e.*, the Sur-tax in respect of 1946-47 is due and payable on 1st January, 1948. As with Income Tax, interest at 3 per cent. per annum is charged on arrears (*see* Chap. II, § 24).

(The tax was at one time known as Super-tax.)

The rates of Sur-tax are normally fixed in arrears, *e.g.*, the rates for 1944-45 were fixed by the Finance Act, 1945. This system cannot be avoided, because the Chancellor of the Exchequer, in framing his Budget, naturally requires any alteration in the rates to be financially effective in the year for which he budgets, not in the following year, as would be the case if the rates of Sur-tax were fixed at the same time as the standard rate.

The Finance (No. 2) Act, 1945, however, departed from this precedent, in fixing the rates for 1945-46 and those for 1946-47, presumably as part of a Budgeting plan.

It must be clearly understood that the sur-tax is an additional tax on individuals. Income Tax is calculated in the ordinary way, and if the statutory total income exceeds £2,000, Sur-tax is also payable.

For 1939-40 to 1945-46 the rates were:—

In respect of—				Rates in £.
The first	£2,000	of total income	.. ..	Nil.
The next	£500	.. ..	.. ..	2/-
..	£500	.. ..	.. ..	2/3
..	£1,000	.. ..	.. ..	3/3
..	£1,000	.. ..	.. ..	4/3
..	£1,000	.. ..	.. ..	5/-
..	£2,000	.. ..	.. ..	5/9
..	£2,000	.. ..	.. ..	7/-
..	£5,000	.. ..	.. ..	8/3
..	£5,000	.. ..	.. ..	9/-
The remainder	.. ..	.. ..	.. ..	9/6

(§ 7—(No. 2) 1940.)

For 1946-47, the rates are as follows:—

In respect of—				Rates in £
The first	£2,000	.. ..	.. ..	Nil.
The next	£500	.. ..	.. ..	2/-
..	£500	.. ..	.. ..	2/6
..	£1,000	.. ..	.. ..	3/6
..	£1,000	.. ..	.. ..	4/6
..	£1,000	.. ..	.. ..	5/6
..	£2,000	.. ..	.. ..	6/6
..	£2,000	.. ..	.. ..	7/6
..	£2,000	.. ..	.. ..	8/6
..	£3,000	.. ..	.. ..	9/6
..	£5,000	.. ..	.. ..	10/-
The remainder	.. ..	.. ..	.. ..	10/6

(§ 15—(No. 2) 1945.)

### Illustration.

Statutory Total Income	.. ..	£15,000
		<u>1946-47.</u>
		£ s. d.
£2,000		—
500 at 2/-	.. ..	50 0 0
500 „ 2/6	.. ..	62 10 0
1,000 „ 3/6	.. ..	175 0 0
1,000 „ 4/6	.. ..	225 0 0
1,000 „ 5/6	.. ..	275 0 0
2,000 „ 6/6	.. ..	650 0 0
2,000 „ 7/6	.. ..	750 0 0
2,000 „ 8/6	.. ..	850 0 0
3,000 „ 9/6	.. ..	1,425 0 0
<u>£15,000</u>		
Sur-tax payable	.. ..	<u>£4,462 10 0</u>

Due 1st January, 1948.

In the case of a deceased taxpayer, the rates of Sur-tax for the year of death will not usually be known until the Budget is introduced in the following April. It is therefore provided that the liability for the year of death can be calculated at the rates applicable to the preceding year (§ 26—1930). If the rates go up, the new rates will not apply, but if the rates go down, the estate benefits from the new rates.

This enables an executor to proceed with the distribution of the estate knowing that he has reserved adequately for Sur-tax by computing it at the rates for the previous year (which he knows), whereas if a reduction is made for the year of assessment in which the death occurred, the estate will benefit. Were it not for this provision an executor would have to wait for the following Finance Act before he knew the full liability.

In normal cases, Sur-tax is charged on the statutory total income as already computed for Income Tax purposes. In arriving at this, care must be taken to ensure that only the *final* statutory total income is taken into account, *e.g.*, where relief has been claimed under § 34, or where the Schedule A assessment is reduced by a claim in respect of repairs, maintenance, etc.

The annual charges to be deducted in arriving at the statutory total income are "those which for taxation purposes are treated as income not of the payer but of the recipient, in respect of which the latter has to bear the tax" (Lord Warrington in *Howe v. C.I.R.* (1919), 2 K.B. 336), *i.e.*, the charges from which the claimant can deduct tax. Annual payments under an oral agreement are deductible if capable of proof (*Peters' Exors. v. C.I.R.* (1941), T.R. 115).

Interest on mortgage paid to a Building Society, interest paid to banks, etc., on overdrafts and loans

(on which Income Tax can be reclaimed—see Chap. IX, § 6), are also deducted as if they were annual payments.

Where applicable, however, deductions may be made in arriving at the income chargeable to Sur-tax as follows :—

(1) If the taxpayer is paying interest on death duties, *e.g.*, where he is paying the Estate Duty on Realty by yearly or half-yearly instalments, he is allowed to regard the interest paid as a net sum, and to deduct the gross equivalent from his income for Sur-tax purposes.

(2) A specific deduction is allowed in respect of any sum which the Treasury may allow for expenses in connection with a person in the service of the Crown abroad, which are necessarily incidental to the discharge of the functions of office, and for which no allowance has already been made (§ 42 (5)—1927). (*See also* § 18—1943.)

(3) Trust expenses may be deducted in the circumstances explained in Chap. XI, § 12.

It must be borne in mind that Sur-tax is payable on total income; no personal or similar allowances can be deducted (§ 40—1927).

See Appendix XIII for relief in respect of diminution of earned income owing to circumstances connected with the 1939-45 War.

## § 2.—The Assessment of Sur-Tax.

### (a) Assessment.

Sur-tax is assessed and charged by the Special Commissioners in one sum and not on separate assessments for each source (§ 42 (2)—1927).

The Special Commissioners may make an assessment or additional assessment in respect of Sur-tax during any time within the year of assessment, or within six years thereafter (or later in case of fraud

or wilful default, *see* Chap. XI, § 18). In normal circumstances, the assessment is made in the year following the year of assessment, as the amounts of the individual's income are not known before. Section 24, 1923 (which provides for relief in respect of error or mistake) applies to Sur-tax (§ 42 (3)—1927). (*See* Chap. II, § 31.)

Where an assessment to Income Tax has become final and conclusive for any year, the assessment is also final and conclusive for the purpose of Sur-tax for that year. No allowance or adjustment of liability on the ground of diminution of income or loss can be taken into account for Sur-tax, unless it has first been made in respect of Income Tax (§ 42 (4)—1927).

Assessments in respect of Sur-tax are subject to appeal to the Special Commissioners. The appeal must be made within 28 days from the date of service of the notice of assessment, or such further date as the Special Commissioners may allow, and must specify the grounds of appeal (S.R. & O. No. 610 (1928) (5)).

Notwithstanding that an appeal is pending, such part of the tax assessed as appears to the Special Commissioners not to be in dispute is collectible as if no appeal were pending. On the determination of the appeal any balance of tax chargeable in accordance with the determination must be paid, or any tax overpaid will be repaid (§ 24—1930).

Even if the recipient of income resides outside the United Kingdom, he is assessable to Sur-tax if the income liable to Income Tax in the United Kingdom exceeds £2,000.

The Special Commissioners have jurisdiction to serve outside the United Kingdom either a notice requiring a return of income arising in the United

Kingdom, or a notice of assessment to Sur-tax (*C.I.R. v. Huni* (1923), 2 K.B. 563).

Where income is taxed at the source, the amount returnable is the gross amount, *i.e.*, the sum received increased by the amount of Income Tax appropriate thereto. (*See* Chap. IV, §§ 12-13.)

Where annual interest is not received, no Sur-tax assessment can be raised thereon even though it is due (*Lambe v. C.I.R.* (1933), 18 T.C. 212). Payment, and not ability to pay, is thus the criterion of liability.

"If there is no interest paid, there is no income to deduct from, and nothing to assess.....but if in a later year the debtor pays the arrears of interest, the payment may be referred to each of the years in which the interest was receivable, and the recipient will be liable to assessment in respect of each of those years" (*ibid.*).

In arriving at the statutory total income of any person :—

- (i) any income which is chargeable with Income Tax by way of deduction at source is deemed to be income of the year in which the income is payable ;
- (ii) any deductions which are allowable on account of annual charges payable under deduction of Income Tax are allowed as deductions in respect of the year in which they become payable.

The period of accrual of the income or charges must be disregarded (§ 39 (2)—1927).

**(b) Adjustment where more than one year's income is receivable in the year of assessment.**

Under the above rule, more than one year's income may be "receivable" in one year of assessment, *e.g.*, where a company declares its yearly dividends just after 5th April in one year and just before 5th April



in the next. The graduation of the Sur-tax rates might make the tax payable as a result very heavy, and provision is therefore made whereby the hardship may be overcome.

Where it can be shown—

- (i) that the income for any year represents more than the income attributable to a full year if the income were deemed to have accrued from day to day, and
- (ii) that in consequence the Sur-tax payable for that year is more than 5 per cent. in excess of the Sur-tax which would have been payable if the income had been deemed to accrue from day to day,

the Special Commissioners must adjust the liability to Sur-tax for that year, and any succeeding year, so as to give such relief as may be just. They must take into account, however, any additional Sur-tax that would have become payable as a result of apportioned income being added to the total income of previous years (§ 34—1927). (*See* § 2 (d)—§ 36—1927.)

The Special Commissioners have an absolute discretion to continue the process of throwing the income back year by year so far as they think it necessary to do justice (*George Gollin v. C.I.R.* (1943), T.R. 69).

#### Illustration.

The following statement shows the statutory income of A for the years 1945-46 and 1946-47 :—

	1945-46. £	1946-47. £
House owned and occupied (Net Annual Value) .. ..	80	85
Interest assessed under Case III ..	150	125
Directors' Fees .. ..	1,000	1,200
Salary as Managing Director ..	1,500	1,500
Dividends (gross amount) .. ..	6,350	7,150
Total .. ..	<u>£9,080</u>	<u>£10,060</u>

Included in the £7,150 dividends for 1946-47 are two years' dividends of £500 each on 6% Preference Shares in A B Ltd., the first having been received on 10th April, 1946, and the second on 31st March, 1947. Compute the Sur-tax payable for the two years, and show what relief can be obtained.

SUR-TAX COMPUTATIONS.			1945-46.	1946-47.
			£	£
Statutory Total Income ..			<u>9,080</u>	<u>10,060</u>
			1945-46.	1946-47.
			£ s. d.	£ s. d.
£2,000 ..			—	—
500 at 2/- ..	50	0 0	500 at 2/- ..	50 0 0
500 „ 2/3 ..	56	5 0	500 „ 2/6 ..	62 10 0
1,000 „ 3/3 ..	162	10 0	1,000 „ 3/6 ..	175 0 0
1,000 „ 4/3 ..	212	10 0	1,000 „ 4/6 ..	225 0 0
1,000 „ 5/- ..	250	0 0	1,000 „ 5/6 ..	275 0 0
2,000 „ 5/9 ..	575	0 0	2,000 „ 6/6 ..	650 0 0
1,080 „ 7/- ..	378	0 0	2,000 „ 7/6 ..	750 0 0
			60 „ 8/6 ..	25 10 0
<u>£9,080</u>			<u>£10,060</u>	
	<u>£1,684</u>	<u>5 0</u>		<u>£2,213 0 0</u>

Had the accrued dividend only been brought into account in 1946-47, the total income would have been reduced by £500 and the Sur-tax by—

	£	s.	d.
£60 at 8/6 ..	25	10	0
440 at 7/6 ..	165	0	0
<u>£500</u>	<u>£190</u>	<u>0 0</u>	

Had Sur-tax been paid only on the basis of the accrued income, it would have amounted to £2,213 less £190 = £2,023. The difference in Sur-tax of £190 exceeds 5% of that amount, and relief will be allowed as follows:—

	£	s.	d.
Reduction for 1946-47 as above ..	190	0	0
Less: Additional Sur-tax for 1945-46 on			
£500 accrued in that year:			
£500 at 7/- ..	175	0	0
Relief ..	<u>£15</u>	<u>0 0</u>	

The Sur-tax for 1946-47 will therefore be reduced by £15 0s. 0d.

(c) *Dealings cum and ex dividend.*

As income taxed by deduction must be included as income of the year of assessment in which it is receivable, the whole dividend paid on stocks purchased "full of dividend" is income of the recipient, although he paid in the purchase price of the stock for the right to the amount accrued. Similarly, Sur-tax would be avoided by selling stocks "full of dividend."

In order to mitigate the loss of Sur-tax to the Revenue on the one hand and the unfair charge on the other, provision is made for the accrued income to be brought into account, as explained hereunder. The restrictions should be noted.

(i) *Where less than the accrued income is received.*

With a view to preventing the avoidance of Sur-tax by habitual dealings in investments *cum* dividend, the Special Commissioners can require any individual to furnish them with a statement showing particulars of his dealings with assets in such a way that either no income had been received, or the amount of income received was less than the income for the period of the holding if the income had been calculated as accruing from day to day.

If, from the statement, it appears that Sur-tax would be avoided to the extent of MORE THAN 10 PER CENT. for any year, the income from the assets shall be treated as having accrued from day to day, and as part of his statutory total income for purposes of Sur-tax, such income being regarded as received as and when it is deemed to have accrued.

If, however, the taxpayer can show—

- (i) that the avoidance of Sur-tax was exceptional and not systematic, *and*

(ii) that there had been no such avoidance in the three preceding years, he is not liable to assessment under this section (§ 33—1927).

The term “assets” for these purposes means—

(1) Stocks or securities, entitled to interest or dividend at a fixed rate only, but excluding stocks or securities on which the interest or dividend is dependent on the earnings of the company.

(2) Any other stocks or securities and any shares if the transactions have not been effected through a Stock Exchange in the United Kingdom and by a transfer bearing 1% stamp duty (§ 33—1927).

It should be noted that no assessment can be raised under § 33, 1927, where the avoidance of Sur-tax was exceptional and not systematic, and it has been held that where the owner of shares avoided Sur-tax in one year by a number of sales, but there had been no avoidance by him in any of the three previous years, he was protected by this provision; a single avoidance of tax is not systematic but exceptional, and the fact that there was a number of sales did not make it systematic (*Bilsland v. C.I.R.* (1936), 20 T.C. 446).

(ii) *Where more than the accrued income is received.*

Where the taxpayer proves that by reason of the acquisition of assets, the amount of Sur-tax payable EXCEEDS BY MORE THAN 10 PER CENT. the amount of Sur-tax which would have been payable for that year if the income from those assets and any assets sold or transferred by him had been treated as accruing from day to day, then, for purposes of assessment to Sur-tax for that year, the income from the assets shall be treated as accruing due from day to day, and received by the taxpayer as and when it is deemed to have accrued (§ 35—1927).

It is important to note that in arriving at the relief, the Sur-tax effect of *all* assets bought and sold in the year must be considered ; a claim cannot be made by reference to one such asset only.

The term "assets" is not defined for the purposes of § 35, nor are there any restrictions similar to those stated above for § 33.

**(d) Ascertainment of "accruing income" for the purposes of Sections 33, 34 and 35—1927.**

Income which is deemed to have accrued from day to day or which is to be computed as if it were income that accrued from day to day shall—

- (a) if payable in respect of any stated period be deemed to have accrued from day to day during that period ; and
- (b) if not payable in respect of any stated period, be deemed to have accrued from day to day during the twelve months preceding the date on which that income was declared payable, or during the period between the last previous declaration of a dividend (not being expressed to be an interim dividend in respect of a stated period), payment of interest, or other yield or produce of such asset and the date aforesaid, whichever period is less.

The usual provisions relating to appeals against assessments to Sur-tax apply (§ 36—1927).

**Illustration.**

A bought £40,000 3½% War Stock, *cum div.* on 20th April and sold it on 2nd June. On 1st June A received a dividend of £700 for the half-year, and this must be included in his statutory income, although he only held the stock for six weeks. If, as a result, his Sur-tax liability was increased by more than 10% over what it would have been had only six weeks' proportion of the dividend been taxable, A can claim the accruals basis, as above.

Similarly, if B purchased  $3\frac{1}{2}\%$  War Stock, *cum div.* on 2nd December, and sold it on 20th April following, so that he had held it for 20 weeks but actually received no dividend, the Revenue could apply § 33, 1927, but only if such avoidance was systematic and not exceptional, and there had been similar avoidance in the preceding three years.

### § 3.—Bonus Shares, etc.

#### (a) Bonus Shares.

A bonus distributed out of accumulated profits, to be satisfied by the issue of fully paid shares in the company, is a capital distribution; it is within the power of the company so to convert its accumulated profits into capital as to make the transaction one of capital against the whole world, including the Crown. Such shares therefore cannot be assessed to Sur-tax in the hands of the individual shareholders taking them (*C.I.R. v. Blott; same v. Greenwood* (1921), 2 A.C. 171). Similarly, where a company issues its capitalised profits in the form of shares, even if an option is given to the shareholder to receive the value of the shares in cash, a shareholder who elects to receive them in shares is not liable to be assessed to Income Tax or Sur-tax in respect of them (*C.I.R. v. Wright* (1926), 95 L.J.K.B. 694).

If, however, shares in another company are distributed, such shares having been acquired out of accumulated profits, they represent income liable to Sur-tax (*Wilkinson v. C.I.R.* (1931), 16 T.C. 52). The position might be different if the shares so acquired were required in the balance sheet to answer share capital (*ibid*).

It appears, therefore, that if there is a release of assets of the company in paying the bonus, the recipient is liable to Sur-tax thereon; if there is no

release of assets, but merely a change of the form of the shareholder's interest in the company, Sur-tax is not attracted.

**(b) Bonus Debentures.**

Profits distributed among the shareholders in the form of an issue of debenture stock, without any option to receive cash, are likewise capital, and the stock received by a shareholder is not liable to assessment to Sur-tax (*C.I.R. v. Fisher's Executors* (1926), 95 L.J.K.B. 487).

**(c) Distribution in Liquidation.**

That portion of the property of the company which represents undistributed profits held in reserve does not form part of the income, for Sur-tax purposes, of the shareholder to whom it is distributed by the liquidator (*C.I.R. v. Burrell* (1924), 93 L.J.K.B. 709), apart from any liability there may be upon undistributed profits of companies to which § 21, 1922 (as amended), applies. (See Chap. VIII, § 7.)

**(d) Profits prior to Incorporation.**

Where a company takes over a business from a date prior to incorporation, or prior to the date of the vending agreement, the profits made prior to the date when the business *de facto* changed hands are assessed upon the vendors, although they may, by the agreement, belong to the company.

The actual date when the company takes over the business, in the eyes of the law, is not necessarily the same date as that mentioned in the agreement. ". . . . the point is not when the contract became a binding contract necessarily. The question is whether there was a succession *de facto* to the business" (*Todd v. Jones Bros.* (1930), 15 T.C. 396).

Any dividend paid for the year in which the business is acquired will, to the extent that the dividend relates to a period prior to the *de facto* date of acquisition, be exempt from Sur-tax, being paid out of profits already assessed upon the vendors (*C.I.R. v. Roberts* (1925), 9 T.C. 603).

#### § 4.—Life Assurance Contracts and Sur-tax.

Prior to 1930, a practice had grown to considerable dimensions whereby Sur-tax was avoided by means of single premium life assurance contracts. The major part of the premium would be paid by means of a loan from the company, on which interest was payable. This interest was an annual charge which reduced the statutory total income of the taxpayer.

To prevent the extension of the practice, it is provided that in computing for Sur-tax purposes the total income for any year of an individual who has entered into a contract of assurance, no deduction is to be allowed in respect of any interest on any borrowed money which has been applied directly or indirectly to or towards the payment of any premium under that contract, or of any sum paid in lieu of any such premium.

Where the benefit of a contract of assurance entered into by any person has become vested in another individual, the restriction applies in relation to that individual—

(a) as if the contract had been a contract entered into by him ;  
and

(b) in a case where the benefit of the contract became vested in him by virtue of an assignment and any payment was made by him in consideration of the assignment, as if that payment were the payment of a premium under the contract ; and

(c) in a case where, either as being the person in whom the said benefit is vested, or by reason of any agreement under or in pursuance of which the said benefit became vested in him, he pays any interest on any borrowed money, as if that money had been applied to the payment of a premium under the contract.



Where, however, the interest is payable at a rate not exceeding ten per cent. per annum, the restriction does not apply to the interest payable in the following cases, and the interest so paid is allowed as a deduction for Sur-tax purposes :—

(a) interest on borrowed money applied to or towards the payment of any premium under a contract of assurance entered into before the 15th April, 1930, which assures a fixed capital sum payable either—

- (i) on death only ; or
- (ii) on the expiration of a period of not less than ten years from the date of the commencement of the contract or on earlier death ;

(b) interest on money borrowed before the 6th April, 1929, unless—

- (i) the money was borrowed from an assurance company ; and
- (ii) the repayment thereof was secured on a contract of assurance ; and
- (iii) the premium in question was a premium under that contract ;

(c) interest on money borrowed mainly on the security of property other than a contract of assurance, if the premium in question either—

- (i) is payable under a contract of assurance entered into in order to provide against the failure of a contingent interest in any property, and to serve as additional security for the loan and for no other purpose ; or
- (ii) is the first of a series of premiums payable under a contract of assurance entered into solely in order to provide for the repayment of the money borrowed and does not exceed ten per cent. of the sum assured under that contract ;

(d) interest on borrowed money applied to or towards the payment of premiums under a contract of assurance which assures throughout the term of the contract a capital sum payable on death, if neither the amount of the first premium under the contract nor the amount subsequently payable by way of premiums thereunder in respect of any period of twelve months exceeds one-eighth of the capital sum payable on death ;

(e) interest on borrowed money applied to or towards the payment of premiums (not being premiums such as those specified in the preceding paragraphs of this subsection) each of which is one

of a series of equal premiums payable at equal intervals of not more than one year, except so far as such interest exceeds in the year of assessment one hundred pounds in all.

The Special Commissioners are empowered to require such particulars with respect to deductions and otherwise as they may consider necessary for the purpose of carrying the restriction into effect.

For these purposes—

(a) the expression “contract of assurance” means a contract of assurance or a contract similar in character to a contract of assurance, being in either case a contract under which a capital sum is expressed to be payable in the future in return for one or more antecedent payments, and the expression “premium” means any such antecedent payment;

(b) the expression “interest” includes any sum payable in respect of any borrowed money;

(c) any reference to borrowed money applied to or towards any payment is deemed to include a reference to borrowed money applied directly or indirectly to or towards the replacement of any money so applied;

(d) any reference to a capital sum payable on death under a contract of assurance is to be construed as a reference to the actual capital sum assured on death, exclusive of any addition which has arisen or may arise from any bonus, share of profits, return of premiums or otherwise, and in the case of a contract under which different capital sums are payable on death in different events, as a reference to the least of those sums (§ 13—1930).

### § 5.—The preparation of a Statement for Sur-Tax purposes.

The question as to whether or not a person is liable to payment of Sur-tax depends upon his statutory total income of the year.

The following formula will be found useful in the preparation of statements for Sur-tax purposes:—

- (1) Collect together the whole of the statutory income from all sources whatsoever, including wife's income (if any), as required in order

to arrive at the total income for Income Tax purposes. Business assessments must be included at the net figure after applying loss claims.

- (2) Deduct annual charges, such as ground rent, mortgage interest, etc., and any interest payable to a banker, or stockbroker, or discount house; interest paid to a building society; and the grossed equivalent of any interest on death duties paid by the taxpayer.
- (3) Deduct in respect of any land on which Income Tax is charged on the annual value, the amount upon which duty has been repaid under Schedule A, No. 5, Rule 8, in respect of the cost of maintenance, repairs, insurance, management, etc.
- (4) Deduct any sum which the Treasury may allow for expenses in the case of a person in the service of the Crown abroad, which are necessarily incidental to the discharge of the functions of office, and for which allowance has not already been made.
- (5) The result represents the statutory total income, and if it is over £2,000, Sur-tax must be paid at the appropriate rates.

If adjustments are necessary under §§ 33, 34 or 35—1927, the formula must be modified accordingly.

Working on the basis of the above formula, the following illustration shows the method by which the correct results may be obtained.

#### **Illustration.**

The following particulars are given in the Income Tax Returns of X :—

	1946-47 Return (Income of 1945-46). £	1947-48 Return (Income of 1946-47). £
Profits of Business .. ..	1,000	1,500
Directors' Fees .. ..	500	600
War Loan Interest .. ..	300	300
Foreign Securities .. ..	900	1,000
Share of Partnership Profits—		
Earned .. ..	1,100	1,200
Unearned (Dividends) ..	450	400
„ (Bank deposit in- terest) .. ..	10	8
Leasehold House, Net Annual Value .. ..	100	120
Schedule B assessment (amenity land) .. ..	4	5
Dividends (including those of wife)	1,300	1,600
Wife's income from trust (gross amount) .. ..	<u>300</u>	<u>260</u>
Annual Charges :—		
Ground Rent on House ..	20	20
Interest on Overdraft ..	40	50

Compute his Sur-tax liability for 1946-47.

SUR-TAX COMPUTATION, 1946-47.

	£	Based on
Business .. ..	1,000	Assessment (previous year's profit).
War Loan Interest .. ..	300	
Foreign Securities .. ..	900	
Directors' Fees .. ..	600	Assessment (actual year's income).
Partnership—		
Earned .. ..	1,100	Share of assessment (previous year's income).
Bank Interest .. ..	10	do. do.
Dividends .. ..	400	Share of dividends for year.
Leasehold House .. ..	120	Sch. A, N.A.V. of year.
Schedule B .. ..	5	One-third G.A.V. of year
Dividends .. ..	1,600	Actual receivable in year.
Trust Income .. ..	<u>260</u>	do.
	6,295	
Less Annual Charges—		
Ground Rent .. ..	£20	Actual payable in year.
Bank Interest .. ..	50	do.
	<u>70</u>	
Statutory Total Income .. ..	<u>£6,225</u>	

## Chargeable—

					£	s.	d.
£2,000	..	..	..	..			
500	at	2/-	..	..	50	0	0
500	„	2/6	..	..	62	10	0
1,000	„	3/6	..	..	175	0	0
1,000	„	4/6	..	..	225	0	0
1,000	„	5/6	..	..	275	0	0
225	„	6/6	..	..	73	2	6
Total .. ..					£860	12	6

Payable 1st January, 1948.

NOTE.—The method of arriving at the Statutory Total Income by extracting the relevant information from two Returns should be observed.

### § 6.—Sur-Tax on the Income of Married Women.

The income of the wife is deemed to be income of the husband for Sur-tax purposes, and the assessment on the combined incomes will be made upon the husband.

If, however, application is made before the 6th July in the year next following the year of assessment, separate assessments will be made (§ 42 (9)—1927). The election will hold good for subsequent years until revoked by similar application (§ 22—1930). The income of the husband and wife is still treated as one in arriving at the tax payable, but the tax is divided between husband and wife in proportion to the amounts of their respective total incomes (§ 42 (9) (b)—1927). An assessment may be made direct on a married woman living apart from her husband (*Brooke v. C.I.R.* (1917), 7 T.C. 261). A husband cannot be assessed to Sur-tax in respect of his wife's pre-nuptial income, since it does not form part of his statutory total income.

#### Illustration.

A married in August, 1946. His own statutory income for 1946-47 was £1,800. His wife had a statutory income of £5,000, of which £2,100 was in respect of the period April to August (prior to marriage). A's statutory total income for 1946-47 is £1,800 + £2,900 (wife's income) = £4,700.

Sur-tax payable :—

£2,000		Nil.
500 at 2/-	..	£50 0 0
500 „ 2/6	..	62 10 0
1,000 „ 3/6	..	175 0 0
700 „ 4/6	..	157 10 0
<u>£4,700</u>	Total ..	<u>£445 0 0</u>

If they claim separate assessments, then

A will pay $\frac{1}{4}\frac{8}{7}$ of £445	.. ..	=	£170 8 6
and his wife will pay $\frac{3}{4}\frac{9}{7}$ of £445	.. ..	=	274 11 6
			<u>£445 0 0</u>

The wife is personally liable on her income prior to marriage, *i.e.*, on £100 at 2/- = £10.

## § 7.—Sur-Tax on undistributed Income of certain companies.

### (a) Provisions applicable to all types of Companies.

Prior to 1922, Sur-tax was payable only on income received by an individual. Consequently, where assets were transferred by an individual to a company and the income from those assets was accumulated, no Sur-tax was payable in respect of that income. Individuals were taking advantage of this method of avoiding Sur-tax, and amending legislation was introduced from time to time to close the loopholes.

The Finance Act of 1922, Section 21 (as amended and extended by the Finance Acts of 1927, 1928, 1936, 1937 and 1939) provides that if a company of the type concerned does not distribute a reasonable proportion of its profits within a reasonable time after the end of its financial year, the whole of its income is to be deemed to be income of its members, and Sur-tax is to be charged on that income as if it had been distributed. The number of decisions of the Court

under these provisions is so large that no attempt has been made to include them here ; indeed, most of them have no general interest, being on special devices contrived in the (usually abortive) attempt to by-pass the legislation.

*Companies affected by the section.*

Any body incorporated in any part of the United Kingdom under any enactment, provided it is—

- (1) Under the control of not more than five persons ;
- (2) Not a subsidiary company ;
- (3) Not a company in which the public are substantially interested.

*Control by not more than five persons.*

A company is deemed to be under the control of not more than five persons—

(1) If any five or fewer persons together exercise, or are able to exercise, or are entitled to acquire, control, whether direct or indirect, over the company's affairs ;

(2) If any five or fewer persons together possess, or are entitled to acquire, the greater part of the share capital or voting power of the company ;

(3) If any five or fewer persons together possess, or are entitled to acquire, either the greater part of the issued share capital of the company, or such part of that capital as would, if the whole income of the company were in fact distributed to the members, entitle them to receive the greater part of the amount so distributed ;

(4) If not more than five persons would have apportioned to them over half the income of the company in the event and on the assumption that it and any other company or companies are liable to a direction under § 21. [In this case, to see whether the company is liable under the Section, it is first necessary to assume that it is liable. Then, if an apportionment of its income would result in over half going to five or fewer persons, the company is deemed to be under the control of not more than five persons.]

For the above purposes, persons who are relatives (husband, wife, ancestor, lineal descendant, brother or sister) of one another, persons who are nominees of any other person together with that other person, persons in partnership, and persons interested in any shares, etc., of the company which are subject to any trust or are part of the estate of a deceased person, are respectively treated as a single person (§ 19—1936).

*Subsidiary Company.*

The term “subsidiary company” is given a special meaning for this purpose. A subsidiary company is one which, by reason of the beneficial ownership of shares therein, is under the control of a company (or companies) to which the Sur-tax provisions do not apply. If, however, the company is under the control of five or fewer persons, it will not be deemed to be a subsidiary company unless it can only be deemed to be under the control of five or fewer persons by including as one of such persons a company to which the Sur-tax provisions do not apply, and which is not the nominee of any other person (*i.e.*, if the minority includes a company to which § 21, 1922 (as amended) does not apply, and which is not a nominee of any other person, and the subsidiary is still under the control of five or fewer persons, it is caught in the net, but if it is not under such control unless such a company is counted in the five, it escapes).

*Public substantially Interested.*

A company is deemed to be one in which the public are substantially interested, if shares of the company (not being shares carrying a fixed rate of dividend) carrying not less than 25% of the voting power have been unconditionally allotted to, or acquired by, *and*



at the end of the year were beneficially held by the public (excluding a company to which these provisions apply), *and* such shares have been dealt with on a Stock Exchange *and officially* quoted during the year.

*Sur-tax directions.*

Companies which are not under the control of five or fewer persons, subsidiary companies (as specially defined), and companies in which the public are substantially interested (as defined) are outside the purview of Sur-tax altogether. Companies which are within the defined limits, however, are all subject to scrutiny by the Special Commissioners, and if they consider that there has been avoidance of Sur-tax by the unreasonable withholding of profits from distribution, they may "direct" that the profits be apportioned among the members.

The precise circumstances should be noted, *viz.*—

Where the Special Commissioners are satisfied that the company has not, WITHIN A REASONABLE TIME AFTER THE END OF ITS ACCOUNTING PERIOD, distributed a reasonable part of its income IN SUCH A WAY AS TO RENDER SUCH INCOME LIABLE TO BE INCLUDED IN THE RECIPIENTS' INCOME FOR PURPOSES OF SUR-TAX, the Commissioners may direct that the WHOLE of the company's income for the year be treated as income of the members, and apportioned among them. (If, therefore, profits have been capitalised and used to pay up bonus shares, which do not constitute income which is taxable in the hands of the recipient, there has been no distribution of the profits for the purposes of Section 21, and if the non-distribution cannot be proved to be "reasonable," a direction can be made.)

Sur-tax will then be assessed and charged on the amount apportioned, after deducting any amount actually distributed by the company. The income is deemed to be received on the date to which the accounts were made up, unless, on application by the company, the Special Commissioners deem some other date to be just, *e.g.*, to avoid the inclusion of more than one year's income in one year's assessment.

*Reasonable Distribution.*

In determining whether a company has distributed a reasonable part of its income, the current requirements of the company, and the necessity or advisability of providing for maintenance and development of the business is to be considered (§ 21 (1)—1922), but the following payments shall be considered as income available for distribution, and not as being applied to current requirements, *viz.*,

- (1) Payments for the business, undertaking, or property which the company was formed to acquire or which was the first business, etc., of a substantial character acquired by the company.
- (2) Repayment of any share or loan capital or debt (including any premium thereon) issued or incurred in payment for any such business, etc.
- (3) Payments in meeting any obligations in respect of the acquisition of such business, etc.
- (4) Any sum applied in redemption or repayment of any share or loan capital or debt (including any premium thereon), issued or incurred otherwise than for adequate consideration.

For this purpose, share or loan capital or debt is deemed to be issued or incurred otherwise than for adequate consideration if—

(a) it is issued or incurred for consideration the value of which to the company is substantially less than the amount of the capital or debt (including any premium thereon); or

(b) it is issued or incurred in or towards, or for the purpose of raising money applied or to be applied in or towards, the redemption or repayment of any share or loan capital or debt which itself was issued or incurred for such consideration as is mentioned in (a) or which represents, directly or indirectly, any share or loan capital or debt which itself was issued or incurred for such consideration. (References to money applied or to be applied for any purpose include references to money applied or to be applied in or towards the replacement of that money.)

(5) Any payments in pursuance of any fictitious or artificial transactions.

It is therefore a question to be determined by reference to the accounts and all the circumstances surrounding the case as to whether the company has in fact distributed a “reasonable” dividend.

The object of the legislation is not to penalise companies which retain undistributed profits for the development and running of the business, but to prevent avoidance of Sur-tax by the accumulation of profits which are not so required. If, therefore, the company's liquid resources are such that it would be impossible or imprudent to distribute the profits, no direction could be sustained. An expanding business often needs every penny of profits for purchasing stocks and giving credit to debtors, purchasing new plant, maintaining fixed assets, etc., and the Special Commissioners could not regard the non-distribution as other than reasonable in such a case.

*Procedure.*

If the Special Commissioners come to the conclusion that the company is one to which § 21 applies, they can either issue a direction apportioning the income of the company over the members, or demand further particulars from the directors. Those further particulars will consist of a statement of the company's income, a copy of the year's accounts, statements of how the income of the company has been dealt with, and of the names, addresses and particulars of the shareholdings of each of the members and such other particulars as they may reasonably require. In that connection it is necessary to furnish them with details which will enable them to arrive at who are the "persons" who control the company.

Within 28 days of the receipt of the notice of direction, or the demand for further particulars, the directors, if they wish to resist assessment, can make a statutory declaration to the effect that there has been no avoidance of Sur-tax through failure to distribute a reasonable part of the company's income for the period. The declaration will state the amount which is regarded as proper to retain in the business, the amount they propose to recommend as dividend, the amount they have distributed as dividends, and the reasons for the retention with such supporting information as the case requires, *e.g.*, a brief financial history of the company and its capital structure, an analysis of the working capital position, future requirements, etc. It must be sworn before a Commissioner, and it is a document which should be prepared with great care, because it may be that upon the satisfactoriness of this document will depend whether or not a direction is made or proceeded with.

On receipt of the statutory declaration, the Special Commissioners decide whether or not they will take further action. If the statutory declaration satisfies them, they will take no further action, but if it does not, they will certify that fact to the Board of Referees, to whom they send the statutory declaration and their certificate that they think there is a case against the company. They must furnish a copy of the statutory declaration and a copy of their certificate to the Commissioners of Inland Revenue, and within 28 days of the receipt of this certificate the Commissioners of Inland Revenue may submit to the Board of Referees a counter-statement (a copy of which will be supplied to the company).

The Board of Referees must then determine whether there is a *prima facie* case for assessing the company. If they decide there is no case, that finishes the matter, but if they decide there is a *prima facie* case, then the Special Commissioners will issue a notice of apportionment of the income of the company to the members.

On receipt of a notice of apportionment, the company may appeal against the apportionment, within 21 days, to the Special Commissioners. If no statutory declaration has been made, the company can appeal against the direction in the same way. At the appeal, evidence will be taken in the usual manner, both the Crown and the taxpayer being usually represented by their advisers.

If either the company or the Commissioners of Inland Revenue are dissatisfied with the determination of the Special Commissioners on the appeal, they can appeal within 21 days to the Board of Referees, who will rehear and determine the appeal. The decision of the Board of Referees at this stage on a question of fact is final ; on a question of law there is

the usual right to appeal to the Courts. The decision to appeal to the Courts must be made and notified within 21 days.

It is important to remember that there is no onus upon the Crown to prove an intention to avoid Sur-tax. The very fact that the company has not distributed a reasonable dividend within a reasonable time after the end of its financial year is sufficient to involve a charge by the Special Commissioners upon that company. The onus of proving that the directors acted unreasonably in withholding profits from distribution, however, is on the Crown (*Thomas Fattorini v. C.I.R.* (1942), 1 A.E.R. 619). Once the Special Commissioners (or if a statutory declaration has been made, the Board of Referees) have decided that a direction is to be made, the Special Commissioners apportion the income of the company to the members. The income of the company for this purpose is arrived at by adjusting the accounts in the same way as for Income Tax purposes, so as to arrive at the adjusted profits of the period; deducting the wear and tear allowance appropriate to the accounting period (found by splitting the allowances agreed for Income Tax); adding income from other sources, and deducting annual payments. The purpose is to arrive at the actual income of the company for the accounting period according to Income Tax rules, taking an actual instead of any preceding year or other basis. Thus, a company which owns and occupies its premises is required to include in its total income the Schedule A value thereof, as part of its income available for distribution, although in fact no tangible income is received. This is not a hardship, however, as the net annual value is charged in arriving at the profits for Schedule D.

The WHOLE of the company's profits as so ascertained is then apportioned among the members in accordance with their respective interests in the capital or profits or income of the company. (The term "member" for these purposes includes any person having a share or interest in the capital or profits or income of the company.) The whole question of the interpretation of the words which provide for the apportionment will be found fully discussed in *F.P.H. Finance Trust v. C.I.R.* ((1945), T.R. 79). It is not therefore necessarily to the same persons who would have got the profits had they been distributed by way of dividend that the Commissioners will apportion the income. There is no notional declaration of dividend, but an apportionment among the persons really interested in the income in question, for whose benefit the distribution of income has obviously been withheld, and upon whom (usually by voting power) it depended whether or not the income should be withheld. The Special Commissioners, having apportioned the income among the appropriate individuals, will then compute what additional Sur-tax would have been paid by each individual if he had had this income, as reduced by any amounts already received by him from the company and already charged to Sur-tax. In ordinary straightforward cases, of course, it will be a simple division among the shareholders, but the net has had to be framed to catch many very ingenious schemes.

#### *Companies in Liquidation.*

When a company goes into liquidation, any assets distributed by the liquidator to the shareholders are capital receipts in their hands. The fact that these may really represent accumulated profits does not alter this, so that Sur-tax is not payable on

undistributed profits distributed as surplus assets by a liquidator (*C.I.R. v. Burrell* (1924), 9 T.C. 27). In the case of companies which are within § 21, 1922, however, there are certain statutory modifications of this rule to prevent avoidance of Sur-tax.

Where an order has been made or a resolution passed for the winding-up of a company to which § 21, 1922, applies, the income of the company for the period from the end of the last year or other period for which accounts of the company have been made up to the date of the order or resolution for winding up shall, for the purposes of the section, be deemed to be income of that period available for distribution to the members of the company, and, as respects that period and the next preceding year or other preceding period or periods ending within that next preceding year for which accounts have been made up, the section shall apply as if the words "within a reasonable time" were omitted. It should be noted, however, that even in such circumstances, no direction can be made if it can be shown that there was no avoidance of Sur-tax through failure to distribute a reasonable part of the income.

Any notice required to be served upon a company may, where the company is in liquidation, be served upon the liquidator, who shall be responsible for doing all matters or things required to be done by or on behalf of the company, and for the due payment of any Sur-tax payable by or recoverable from the company.

In connection with bodies corporate which are not companies within the meaning of the Companies Act, 1929—

- (a) references to winding-up include references to the dissolution or cancellation of the registry of the body corporate in any manner authorised by any rules, regulations or



before the expiration of three months from the date of service or before the second day of January following the year of assessment (whichever is the later), the tax thereupon becomes recoverable from the member on whom the tax was assessed without prejudice to the right to recover it from the company.

Interest is chargeable if the tax is not paid within three months of the due date (*see* Chap. II § 24) (§ 8—(No. 2) 1947).

*Subsequent distributions.*

The company should clearly distinguish those reserves which have suffered Sur-tax under these provisions from the reserves which have not suffered Sur-tax, since when any sum is distributed on which Sur-tax has been levied under these provisions, it will be exempt in the hands of the recipient. If the recipient inadvertently pays Sur-tax on any such distribution he can recover it from the Revenue. There is no provision in the Act whereby the company can recover from the individual the Sur-tax it has had to pay on his behalf, except on a distribution of surplus on liquidation (*see* above); the dividends of all members will thus be reduced *pro rata* by reason of the payment of the Sur-tax, irrespective of their respective liabilities.

*Non-Subsidiary Companies.*

Where a company under the control of five or fewer persons is deemed to be "not a subsidiary company," its income is apportionable through intermediate holdings into the hands of the beneficial owners; thus, where a member of a company is itself a company, the income of the first company can be apportioned to that "member" company, and in turn apportioned

amongst the members of that company. These provisions are sufficiently wide to enable the undistributed income to be followed through any chain of companies until the beneficial owner is reached, each company being required to furnish lists of its members and their holdings. In each case, however, the company must come within the definitions attracting liability.

*Submission of accounts to Special Commissioners  
after General Meeting.*

In order to enable a company to ascertain within a reasonable time whether or not it is likely to be subjected to a direction, it may, at any time after the general meeting at which the accounts are adopted, forward a copy of the annual accounts and the directors' report to the Special Commissioners. The Commissioners may, within 28 days of the receipt, request the company to furnish them with further particulars within 28 days or such extended period as they may allow. If, within three months after the receipt of the accounts or further information, as the case may be, the Commissioners do not indicate their intention to take further action, the Commissioners' rights to take action cease. If, however, the Commissioners intimate that they propose to take further action, they must proceed within six months of the date of the intimation (§ 18—1928).

*Expenses of Appeal.*

The expenses of a SUCCESSFUL appeal against Sur-tax will, in practice, be allowed as a deduction in arriving at the company's assessable profits under Schedule D.

**Illustration.**

The available profits, from the point of view of the above provisions, of a company controlled by A, B and C, for the year ended 31st March, 1947, were £18,000, made up as follows :—

Profits as adjusted for Schedule D,

Case I .. .. .	£14,995	
Less Wear and Tear allowance ..	495	
	<u>14,500</u>	£14,500
Schedule A assessment on premises owned		1,500
Untaxed interest .. .. .		400
Dividends received (gross) .. .. .		3,000
		<u>19,400</u>
Less Mortgage interest	£600	
Debenture interest	800	
	<u>1,400</u>	
		<u>£18,000</u>

The share capital was held as follows :—

	Shares of £1 each.
A .. .. .	30,000
B .. .. .	30,000
C .. .. .	10,000
D, wife of A .. .. .	10,000
E, Uncle of B .. .. .	10,000
F, nominee of C .. .. .	10,000
	<u>100,000</u>

B had no control over E.

No dividend was paid, and the Special Commissioners, holding this to be unreasonable in the circumstances, apportioned the profits over the members. A had other income of £5,000; B other income of £1,800; C other income of £500; and E other income of £200.

	A.	B.	C.	E.
Other Income .. .. .	£5,000	£1,800	£500	£200
Proportion of profits applicable to share holding (including wife in the case of A and nominee in the case of C) .. .. .	(40%) 7,200	(30%) 5,400	(20%) 3,600	(10%) 1,800
	<u>£12,200</u>	<u>£7,200</u>	<u>£4,100</u>	<u>£2,000</u>
Sur-tax liability at 2/-	£500	£500	£500	Nil
2/6	500	500	500	—
3/6	1,000	1,000	1,000	—
4/6	1,000	1,000	100	—
5/6	1,000	1,000	—	—
6/6	2,000	1,200	—	—
7/6	2,000	—	—	—
8/6	2,000	—	—	—
9/6	200	—	—	—

The company's liability is therefore at the highest rates attributable to each member, *viz.*,

				£	s.	d.	£ s. d.		
re A	..	£1,000 at 5/6	..	275	0	0			
		2,000 „ 6/6	..	650	0	0			
		2,000 „ 7/6	..	750	0	0			
		2,000 „ 8/6	..	850	0	0			
		200 „ 9/6	..	95	0	0			
		<u>£7,200</u>					2,620	0	0
re B	..	£500 at 2/0	..	50	0	0			
		500 „ 2/6	..	62	10	0			
		1,000 „ 3/6	..	175	0	0			
		1,000 „ 4/6	..	225	0	0			
		1,000 „ 5/6	..	275	0	0			
		1,200 „ 6/6	..	390	0	0			
		<u>£5,200</u>					1,177	10	0
re C	..	500 at 2/-	..	50	0	0			
		500 „ 2/6	..	62	10	0			
		1,000 „ 3/6	..	175	0	0			
		100 „ 4/6	..	22	10	0			
		<u>£2,100</u>					310	0	0
							<u>£4,107</u>	<u>10</u>	<u>0</u>

If and when the profits are ultimately distributed, they are exempted from Sur-tax in the hands of the recipients, although there is no provision whereby the company can recoup the Sur-tax paid from the individuals in question. The company will simply distribute the balance of profits remaining after debiting the total Sur-tax paid, and members not liable to Sur-tax thus actually bear part of the charge.

**(b) Provisions applicable to investment companies only.**

The provisions for assessing undistributed profits in the case of investment companies are even more stringent than those already dealt with, which apply to all companies within the mesh of the net cast by the Acts.

For this purpose, an investment company is defined as any company, the income whereof consists mainly of investment income, that is to say, income which,

if the company were an individual, would not be earned income. Any income apportioned to the company under § 21, 1922, is deemed to be income of the company and to be investment income.

An investment company is deprived of the rights of making a statutory declaration or of submitting accounts with a demand to have its position ascertained. The Special Commissioners may require an investment company to supply any information they may think necessary.

*Profits available for distribution.*

In computing the actual income of an investment company, no deduction is to be allowed which would not be allowable in computing the income of an individual, except that deductions are allowed for such sums disbursed as expenses of management as the Special Commissioners consider reasonable, having regard to the requirements of the company's business and, in the case of directors' fees or other payments for services, to the actual services rendered to the company. N. D. C. and E. P. T. are expenses of management.

*Control.*

The circumstances in which an investment company is deemed to be under the control of five or fewer persons are the same as those detailed in (a) above with the addition of a provision that an investment company is deemed to be under the control of not more than five persons if any five or fewer persons would, if the company were wound up, be entitled as members or loan creditors of the company to receive more than half of the assets of the company which would be available for distribution to members and loan creditors.

The expression "loan creditor" means a creditor in respect of any debt incurred by the company—

- (a) for any money borrowed or capital assets acquired by the company; or
- (b) for any right to receive income created in favour of the company; or
- (c) for consideration the value of which to the company was (at the time when the debt was incurred) substantially less than the amount of the debt (including any premium thereon);

or in respect of any redeemable loan capital issued by the company.

A person carrying on the business of banking is not to be deemed to be a loan creditor in respect of any loan capital or debt issued or incurred by the company for money lent by him to the company in the ordinary course of that business.

Where an investment company is deemed to be under the control of not more than five persons by reason that any five or fewer persons would, if the company were wound up, be entitled as loan creditors to receive more than one-half of the assets (whether or not it would otherwise be deemed to be under such control)—

- (a) the definition of the expression "member" is extended so as to include any loan creditor of the company; and
- (b) for the purpose of apportioning the company's income over the members, a loan creditor is deemed to have an interest in any income of the company to be apportioned to the extent that that income, or assets representing it, has or have been expended or applied or is or are available to be expended or applied in redemption or repayment or discharge of the loan capital or debt (including any premium thereon) in respect of which he is a loan creditor.

Where by virtue or in consequence of any settlement on children within the meaning of § 21, 1936 (*see* Chapter XI, § 5), a

loan creditor has been or could be required by some other person (hereafter referred to as a "beneficiary") to pay to the beneficiary the whole of any sums payable to that loan creditor by the company in redemption, repayment or discharge of the loan capital or debt (including any premium thereon) in respect of which he is a loan creditor, or to pay or transfer to the beneficiary the whole of any sums or assets representing directly or indirectly any such sums, the beneficiary and not the loan creditor is deemed to be a member of the company and, for the purposes of apportioning the company's income, to have the interest in the income of the company which the loan creditor would, but for this provision, be deemed to have ; and—

Where a loan creditor has been or could be required as aforesaid to pay or transfer to the beneficiary a part only of any such sums or assets as aforesaid, the beneficiary, as well as the loan creditor, shall be deemed to be a member of the company and for the purpose of apportioning the company's income, the interest which the loan creditor is deemed to have in the income of the company shall be apportioned by the Special Commissioners between the beneficiary and the loan creditor.

Any person in whose name any loan capital is registered can be required by the Special Commissioners to state whether he is the beneficial owner of the loan capital, and if not the beneficial owner, to furnish the name and address of the real owner.

The Special Commissioners may treat as a member of an investment company for all purposes of § 21, 1922, any person who is, or is likely to be, able to secure that income or assets of the company will be applied either directly or indirectly for his benefit, and may apportion income to him as they consider appropriate. They can only do so, however, if that person has transferred, directly or indirectly, to the company assets the value of which is not adequately represented in the value for apportionment purposes of any relevant interests he has in the company, and the directors or other persons who can dispose of or apply the company's income or assets are persons likely to act in accordance with his wishes.

*Investment Companies in Liquidation.*

Where an investment company to which § 21, 1922, applies goes into liquidation—

(a) the actual income of the company from all sources since the date of the order or resolution is deemed to be the income of the members ;

(b) the Special Commissioners shall from time to time by notice in writing to the liquidator direct that the amount of that income for the year or period specified in the notice shall be deemed to be the income of the members for that year or period, and the amount thereof shall be apportioned and Sur-tax assessed and charged accordingly.

*Apportionment.*

In the case of an investment company, apportionment is automatic, whether or not there has been a reasonable distribution of profits, unless the company exists wholly or mainly for the purpose of carrying on a trade or for the purpose of co-ordinating the administration of a group of trading companies. The Special Commissioners are not to apportion the profits by reference to an accounting date, as for trading companies, but must make the direction by reference to the year of assessment. For this purpose all the income of an investment company is deemed to be available for distribution as soon as it becomes due and payable to the company. Where a company goes into liquidation, the Special Commissioners may treat either of the following periods as if it were a year of assessment—

- (i) the period from the end of the last year or other period for which accounts of the company have been made up to the date of the order or resolution for winding up ; or
- (ii) the period from the end of the last year of assessment to the date of the order or resolution.



The Special Commissioners, if they think fit, can apportion the income, not according to what each member would receive if the income were paid away in dividends, but by attributing to each member an interest corresponding to his interest in the assets of the company available for distribution among the members in a winding-up. This applies to sub-apportionments as well as original apportionments, *i.e.*, income can be followed through a chain of companies (§ 13—1939).

*Investment Companies with Estate or Trading income.*

“Estate or trading income” means income chargeable to Income Tax under Schedule A or Schedule B, income arising in respect of the ownership or occupation of land (including furnished lettings), which is chargeable to income tax under Schedule D, and income which, if received by an individual, would be earned income.

If the whole of the income of an investment company is estate or trading income, a direction can only be made on it where it has not distributed a reasonable proportion of its profits. Any sum expended or applied, or available to be expended or applied, in or towards the redemption, repayment or discharge of any loan capital or debt (including premiums thereon) in respect of which any person is a loan creditor of the company, will be deemed to be available for distribution.

If part of the income of an investment company is estate or trading income—

- (1) The company will be treated as if such part of the income as is not estate or trading income were the whole of its income, and automatic apportionment will apply to that part of the income.

- (2) The estate or trading income will then be reviewed on the assumption that it is the only income of the company, and a direction for apportionment will arise if a reasonable distribution of profits has not been made.
- (3) Any distributions of income made by the company will be deemed to have been made first out of income other than estate or trading income.
- (4) Outgoings are to be attributed to whichever type of income the Special Commissioners consider appropriate.
- (5) If the cost of maintenance, repairs, insurance and management exceeds the gross estate or trading income of the company, the company may, on giving written notice to the Special Commissioners within six months of the end of the year of assessment, require the excess to be deducted from the other income of the company.

The above provisions do not apply after the commencement of winding-up; automatic apportionment will follow that event. Nor do they apply in the case of any company which exists mainly or wholly for the purpose of carrying on a trade or for the purpose of co-ordinating the administration of a group of trading companies.

(See Chap. XII, § 3, as to effect of a direction on Profits Tax).

**§ 8.—Provisions for preventing avoidance of Income Tax by transactions resulting in the transfer of income to persons abroad.**

In order to avoid Income Tax and/or Sur-tax certain individuals ordinarily resident in the United

Kingdom, made transfers of assets by virtue or in consequence of which income became payable to persons resident or domiciled outside the United Kingdom. Section 18, 1936, as amended by § 28 and 5th Sch., 1938, and § 21, 1940, contains provisions intended to stop this form of tax avoidance, enacting that the income is to be treated as income of the individual who has entered into the scheme. The Section comes into operation if—

- (1) there is a transfer of assets by an individual resident in the United Kingdom ;
- (2) an individual has power to enjoy the income payable abroad,

unless the individual can show, to the satisfaction of the Special Commissioners, either (a) that the purpose of avoiding liability to taxation was not the purpose or one of the purposes for which the transfer or associated operations or any of them were effected, or (b) the transfer and any associated operations were *bonâ fide* commercial transactions and were not designed for the purpose of avoiding liability to taxation.

Income received by one person which is required to be regarded as that of another by § 18, 1936, or any similar legislation, is not exempted from tax by any Treasury conditions of issue, or by Gen. Rule 2 of Sch. C, by reason of the recipient of the income not being resident, ordinarily resident or domiciled in the United Kingdom (§ 21 (5)—1940).

As these provisions are of very limited interest, the text of the section (as amended) is reproduced in Appendix X.

### § 9.—Sur-tax on Income of Infants.

An infant whose Statutory Total Income exceeds £2,000 is assessable to Sur-tax. In arriving at the

total income, the whole income from vested funds must be included, even if accumulated; but if part of the income is spent on the infant's maintenance and part accumulated, and the infant is only entitled to such accumulations contingently on his attaining twenty-one, he has no title to the accumulations until that event takes place; the accumulations are not his income in the years in which they accrue and he cannot be assessed to Sur-tax on them. Income accumulating under statutory trusts under § 31, Trustee Act, 1925, is contingent and not assessable to Sur-tax during minority. The effect of this section is to make the income of the settled property different for Sur-tax purposes from what it would have been if the section had never been enacted and to remove it from the category "income of the infant" (*Stanley v. C.I.R.* (1944), T.R. 3). (cf. *C.I.R. v. Countess of Longford*; *Gascoigne v. C.I.R.* (1927), 13 T.C. 573, where the income accrued to the death of the infant would have passed to her legal personal representatives, and was therefore assessable to Sur-tax.)

**§ 10.—Recovery of Sur-tax due from beneficiary under discretionary trust.**

Where Sur-tax is due from any beneficiary to whom or for whose benefit any income or any capital may in the discretion of some other person be paid or applied under a trust, and any Sur-tax charged in respect of the income of the beneficiary is not paid before the expiration of six months from the date when it became due and payable, the Special Commissioners may require the trustees of the settlement to pay the Sur-tax.

The trustees must then, as soon as may be, and, if necessary from time to time, pay to the Commissioners

of Inland Revenue on account of the Sur-tax from time to time remaining unpaid any income or capital which, under the trust, the beneficiary may become entitled to receive or to have applied for his benefit.

Any such payment made out of income by trustees on account of Sur-tax is regarded for all the purposes of the Income Tax Acts as income paid to the beneficiary. .

Where there are two or more trustees under the trust, a notice to pay Sur-tax in such cases is deemed to have been validly served upon the trustees if served upon any one of them, but this does not render a trustee personally liable for anything done by him in good faith and in ignorance of the fact that such a notice has been served (§ 34—1933).

## CHAPTER IX.

## CLAIMS FOR RETURN OF TAX, Etc.

## § 1.—Summary of Claims for Return of Tax.

In those cases where the whole or a major part of an individual's income is from investments, the tax deducted from his income will exceed his liability, having regard to his allowances, and he should claim repayment of the excess tax suffered. A repayment claim can be made at any time within six years after the end of the year of assessment to which the claim relates (§ 30—1923), except where otherwise stated.

Claims for repayment of Income Tax also arise in the cases of—

- (1) Double assessment (§ 151), *e.g.*, where land has been assessed under Sch. B and the profits from the land are also included in business profits assessed under Sch. D.
- (2) A trading loss in the year of assessment (§ 34). This claim must be made within 12 months of the end of the year of assessment (*see* Chap. VII, § 2).
- (3) Charitable institutions and other bodies with income exempt from tax.
- (4) Interest on short loans paid to bankers, stockbrokers or discount houses, and not charged as an expense in the business accounts (§ 36).
- (5) The actual profits from working a farm being less than the statutory assessment under Sch. B (Sch. B, R. 6). This claim must be

made within 12 months of the end of the year of assessment (*see* Chap. III, § 2).

- (6) Maintenance of property under Sch. A (Sch. A, No. V, R. 8) (*see* Chap. III, § 1).
- (7) The appropriate deductions in respect of land tax, tithe redemption annuities, owner's rates, etc., not having been made in arriving at the Net Annual Value (Sch. A, No. V, RR. 1-5).
- (8) Rent irrecoverably lost (§ 204 in Northern Ireland, and by concession in Great Britain) (*see* Chap. III, § 1); the claim must be made within 12 months of the end of the year of assessment.
- (9) Empty property; within 12 months of the end of the year of assessment (Sch. A, No. VII, R. 4) (*see* Chap. III, § 1).
- (10) Income derived from a British Dominion or Possession which has also borne Income Tax in that Dominion or Possession or from a country with whom Great Britain has a double taxation agreement (§ 27—1920) (§ 46—1927) (*see* Chap. X).
- (11) Diminution of Earned Income owing to war causes (*see* Appendix XIII).
- (12) Small maintenance paid under § 25, 1944, without deduction of tax (*see* Chap. XI, § 9).

Various other adjustments are claimable in specific instances, *e.g.*, in respect of new businesses, successions to businesses, etc., which are dealt with *passim*.

## § 2.—Method of making Claim for Repayment.

If the taxpayer has already made a proper return of his total income claiming his reliefs and allowances,

he is not ordinarily required to complete another form. Where no return has been made, however, he will be required to complete a special claim form, giving details of his income, and claiming the allowances to which he is entitled.

Claims for the tax due to be repaid for any year may be made in many cases considerably before 5th April. If his allowances enable the taxpayer to reclaim the *whole* of the tax deducted from dividends, etc., he may claim repayment as soon as all the income, *taxed at the source*, of the year to 5th April has been received.

Other persons entitled to repayment may claim in respect of the reliefs due to them for the year as soon as they have borne for the year sufficient tax to cover the amount of such reliefs.

If desired, an *instalment* of the repayment due for the year may be claimed at intervals convenient to the claimant. On making a claim for an instalment, the taxpayer must give particulars of the income from every source for the year and of the tax thereon actually suffered up to the date of the claim; any income on which tax has not been suffered will be deducted from the allowances due and tax repaid only on the balance of allowances.

Vouchers must be forwarded with the claim showing income, subjected to tax, sufficient to cover the amount of income on which repayment is claimed and the amount of any charges, as tax recoverable by deduction from charges cannot be repaid. In the case of an instalment claim, vouchers should be sent in respect of each item of income, subjected to tax, received up to the date of the claim.

#### Illustrations.

(1) William Johnson has been assessed to Income Tax under Schedule D for year 1947-48 in the sum of £402, as a grocer. He is



married, has two children, aged 10 and 12, and maintains his invalid sister who has an income of £90. His wife has no income, but he has £500 a year gross from taxed dividends. He pays a Life Assurance Premium of £10 on a policy for £500.

If full information as to his income is before the Inspector of Taxes when the assessment is made, the notice might read as follows :—

					Schedule D.
Profits	..	..	..	..	£402
<i>Deduct Allowances :</i>					
Earned Income	..	..	..	..	£67
Personal	..	..	..	..	180
Children	..	..	..	..	120
Dependent Relative	..	..	..	..	30
					<hr/> 397
					<hr/> £5
Chargeable—					£ s. d.
£5 at 3/-	..	..	..	..	15 0
<i>Less Life Assurance Allowance—</i>				£ s. d.	
£10 at 3s. 6d.	..	..	..	1 15 0	
† Deduction of 6/- in £ on £45					
and 3/- in £ on £75 in					
respect of dividends	..	..	..	24 15 0	
					<hr/> 26 10 0
Repayable	..	..	..	..	<hr/> £25 15 0

† Since Johnson is entitled to reduced rate relief on £50 at 6/- and on £75 at 3/- and has only had it on £5 at 3/-, he is entitled to repayment against the investment income which has suffered tax at 9/- to give him the full benefit of the lower rates.

Possibly, however, the tax payable on the assessment would actually be shown as nil, leaving the taxpayer to reclaim, since the repayment would not be made until vouchers had been produced to cover the tax reclaimed.

#### REPAYMENT CLAIM, 1947-48.

		Gross.			Income Tax.		
		£	s.	d.	£	s.	d.
Total Income—							
Dividends	..	..	..	500 0 0	225	0	0
Business	..	..	..	402 0 0			
				<hr/> 902 0 0			
<i>Less Allowances</i>	..	..	..	397 0 0			
				<hr/> £505 0 0			
Carried forward	..				£225	0	0

	£	s.	d.	£	s.	d.
Brought forward ..				225	0	0
£50 at 3/- .. ..	7	10	0			
75 at 6/- .. ..	22	10	0			
380 at 9/- .. ..	171	0	0			
	201	0	0			
Less Life Assurance Allowance						
£10 at 3s. 6d. .. ..	1	15	0			
				199	5	0
Repayment .. ..				£25	15	0

(2) Jones had the following income for 1947-48 :—

Business Profits .. ..	£150
Dividends (net) .. ..	440
Rent of house (assessed under Sch. A at £120) .. ..	90
Net Annual Value of residence held on lease .. ..	100
Wife's income from employment ..	120

He paid ground rent of £40 per annum, and mortgage interest of £60 per annum. (These sums are the gross amounts.) He had two children under 16, and paid £100 in Life Assurance Premiums on policies taken out after 22nd June, 1916. The direct assessments had been discharged, and on 5th April, 1948, Jones submitted his repayment claim. The tax repayable is computed as follows :—

	Income Tax.
Dividends—gross .. .. £800 .. ..	£360 0 0
House let, rent received, being less than N.A.V... 90 .. ..	40 10 0
House in own occupation ..	100
Case I, Sch. D assessment on profits .. ..	150
Sch. E assessment on wife	120
£1,260	Total tax suffered at source
	£400 10 0
Carried forward .. £1,260	£400 10 0

					£	s.	d.
	Brought forward	£1,260			400	10	0
<i>Less</i>	Annual Charges—						
	Ground Rent ..	£40					
	Mortgage Interest	60					
			100	..	45	0	0
	Statutory Total Income	£1,160					
				Tax available for repayment ..	£355	10	0
<i>Deduct</i>	Allowances—						
	Earned Income						
	$\frac{1}{8}$ of £270 ..	£45					
	Personal ..	180					
	Additional Personal	100					
	Children ..	120					
					£445		
	Taxable Income ..				£715		
	Chargeable—						
	£50 at 3/- ..				£7	10	0
	75 at 6/- ..				22	10	0
	590 at 9/- ..				265	10	0
					£295	10	0
<i>Less</i>	Life Assurance						
	Relief—£100 at 3s. 6d.	17	10	0			
	Net liability					278	0 0
				Tax repayable .. ..	£77	10	0

An alternative arrangement (not recommended to students)  
is as follows :—

Claim—					£	s.	d.
Personal Allowance	..	..	£180				
Additional „	..	..	100				
Children	..	..	120				
			400				
<i>Less</i>	Untaxed Income—						
	Business .. ..	£150					
	Wife's Earned	120					
		270					
<i>Less</i>	Earned Income						
	Allowance .. ..	45					
		225					
	House .. ..	100					
		325					
				£75 at 9/-	33	15	0
	Carried forward .. ..				£33	15	0

	£	s.	d.
Brought forward .. .. .	33	15	0
Reduced Rate £50 at 6/- and £75 at 3/- ..	26	5	0
Life Assurance £100 at 3s. 6d. .. .. .	17	10	0
<b>Total claim .. .. .</b>	<b>£77</b>	<b>10</b>	<b>0</b>

(3) A single person over 65 years of age has a total income for 1947-48 as follows :—

	£	s.	d.	£	s.	d.
Pension .. .. .	150	0	0	—		
Dividends (gross amount) ..	100	0	0	45	0	0
	<u>£250</u>	0	0			
<i>Deduct Allowances—</i>						
Old Age $\frac{1}{6}$ th ..	£42					
Personal ..	110					
	<u>          </u>	152	0	0		
		<u>          </u>				
Taxable Income ..	£98	0	0			
	<u>          </u>					
Chargeable £50 at 3/- ..	£7	10	0			
£48 at 6/- ..	14	8	0			
		<u>          </u>		21	18	0
				<u>          </u>		
Repayable .. .. .				£23	2	0

(4) M. White submits the following particulars of his income from all sources for the year 1947-48 :—

He owns and works a small holding. The Gross Annual Value of the lands is £20. The farmhouse is assessed separately at a Net Annual Value of £7 10s. 0d.

He holds £4,400  $2\frac{1}{2}$  per cent. Consols.

He is the proprietor of a business, the adjusted profits of which for the year 1946 were £57. Interest amounting to £35 (gross amount) is paid to X on a loan to the business.

His wife, a director of the Improved Industrial Dwellings, Ltd., receives fees of 56 guineas per annum.

He owns three cottages from which he receives £75 per annum, the gross annual value under Schedule A being £72. The rents are collected by an agent, whose charges amount to £3 15s. 0d., whilst repairs cost £2.

The leasehold shop in which his business is carried on is assessed under Schedule A at a Net Annual Value of £40 net, the ground rent thereon being £10 per annum.

His wife holds shares in the Improved Industrial Dwellings, Ltd., from which she received, free of tax, dividends amounting to £275.

There are mortgages on the properties of £1,000, upon which interest at the rate of  $4\frac{1}{2}$  per cent. per annum is payable.

He is insured for £1,500, at an annual premium of £100, and his wife is insured for £1,000, the premium being £22 per annum.

All tax under Schedule A has been paid, but no tax has been paid under Schedules B, D or E.

He has three children, aged 15, 12 and 9 respectively, none of whom has any income.

M. WHITE—REPAYMENT CLAIM, 1947-48.

Source of Income.					Gross.		Income Tax.	
					£	s. d.	£	s. d.
Farm, Schedule B (£30 × 3)	..	..	..	..	90	0 0		
Business " D	..	..	..	..	57	0 0		
Wife's Director's Fees, Schedule E	..	..	..	..	59	0 0		
Farmhouse and Land, Schedule A (£17 10 0 + £7 10 0)	..	..	..	..	25	0 0	11	5 0
Cottages do.	..	..	..	..	54	0 0	24	6 0
Shop do.	..	..	..	..	40	0 0	18	0 0
Consols Interest	..	..	..	..	110	0 0	49	10 0
Wife's Dividends (£275 × $\frac{1}{4}$ )	..	..	..	..	500	0 0	225	0 0
Total	..	..	..	(a)	£935	0 0	£328	1 0
ANNUAL CHARGES—								
Interest on Loan	..	..	..	..	35	0 0	15	15 0
Ground Rent	..	..	..	..	10	0 0	4	10 0
Mortgage Interest	..	..	..	..	45	0 0	20	5 0
Total	..	..	..	(b)	£90	0 0	£40	10 0
Statutory Total Income ((a) - (b))	..	..	..	..	845	0 0	287	11 0
Deduct Allowances—								
Earned Income (1/10th of £206)	..	..	..	£34				
Personal	..	..	..	180				
Additional Personal	..	..	..	49				
Children	..	..	..	180				
					443	0 0		
Taxable Income	..	..	..	..	£402	0 0		
Chargeable—								
£50 at 3/-	..	..	..	..	7	10 0		
75 at 6/-	..	..	..	..	22	10 0		
277 at 9/-	..	..	..	..	124	13 0		
					154	13 0		
Less Life Assurance Allowance £122 at 3s. 6d.	..	..	..	..	21	7 0		
							133	6 0
Repayable	..	..	..	..			£154	5 0

Alternatively, the claim may be computed :—

		£		
Allowances due—				
Personal	.. ..	180		
Additional Personal	.. ..	49		
Children	.. ..	180		
		<hr/>		
		409		
Less Untaxed Income	.. £206			
Less Earned Income				
Allowance	.. .. 34			
		<hr/>		
		172		
		<hr/>		
		£237 at 9/-	£	s. d.
			106	13 0
		<hr/>		
Reduced Rate, £50 at 3/- and £75 at 6/-	.. ..	26	5	0
Life Assurance	.. ..	21	7	0
		<hr/>		
Repayable	.. ..	£154	5	0

*Notes to Illustration.*

- (1) The repairs allowance on land is one-eighth. The net annual value of the farm land is therefore £17 10s. 0d. to which is added that of the house £7 10s. 0d., giving a total of £25 0s. 0d. for Schedule A. As M. White owns the farm, the net annual value forms part of his statutory income.
- (2) As occupier of the farm, he will be assessed under Sch.B on three times the gross annual value of the land, including the farm house. The G.A.V. of the house is £10 since the repairs allowance is one-quarter.
- (3) In the case of house and cottage property, the statutory repairs allowance covers all expenses in connection with the property; consequently agent's fees and repairs cannot further be taken into consideration. Since the gross annual value of the *three* cottages is £72, *each* is under £40, and the deduction for repairs, etc., is one-fourth. There are no excess rents as the assessment is normally one-twenty-sixth less than the rent in such cases.
- (5) J. W. is a married man with two children, aged 10 and 12 years.

He commenced business as an Estate Agent on 1st July, 1945, and his first accounts, for the nine months to 31st March, 1946,

showed a loss of £120, which was carried forward under § 33, 1926. His next accounts, for the year to 31st March, 1947, showed a profit of £280, and those for the year to 31st March, 1948, a profit of £520.

He was a director of A Ltd. his remuneration for the year to 5th April, 1948, being £750. Income Tax deducted in 1947-48 under P.A.Y.E. was £281 5s. 0d.

His share of the residuary income of an estate for the year ended 5th April, 1948, was £572 after deduction of Income Tax, and this sum was paid to him on 5th April, 1948.

He owned the following properties :—

Mansion House, assessed under Schedule A at £200 net.

Agricultural Land and Buildings of a value of £120 net for Schedule A, and £270 for Schedule B.

Lodge, assessed under Schedule A at £100 net.

The Mansion House was vacant and unfurnished from 6th October 1947, to 30th June, 1948; the Lodge was let at a rent of £75 a year. J. W. himself farmed the agricultural land and submitted accounts for the year ended 31st March, 1948, showing an adjusted loss of £300, in respect of which he made all claims available to him.

He received a full year's income in the year 1947-48 from 30,800 5 per cent. Preference Shares of £1 each. He sold his holding of £200 3½ per cent. War Loan, which he had held for several years on 20th April, 1947.

On a Life Assurance Policy for £15,000, taken out in 1914, he paid a yearly premium of £600.

In the year 1947-48 he paid £525 bank interest.

By arrangement with H.M. Inspector of Taxes, the payment of Income Tax, except that under Schedule E (which was assessed at the standard rate after giving effect to Earned Income Relief) and Schedule A, was suspended pending the settlement of a claim to an appropriate refund in respect of the year ended 5th April, 1948.

Compute the claim, setting out your full workings.

## COMPUTATION, 1947-48.

Schedule D—Case I—	£	£	Tax paid	£	s.	d.
Assessment based on accounts to 31st March						
1947 .. .. .	280					
Less Loss brought forward ..	£120					
Allowed in arriving at assessment for 1946-47 3/12ths of £280	70*	50				
		280				
Schedule E—Assessment .. .. .		750		281	5	0
Income from Estate (net) .. .. .	572					
Add Income Tax .. .. .	468	1,040		468	0	0
Schedule A—Mansion House .. .. .	200		£200 @ 9/-	90	0	0
Less "Void" Claim, 6 months .. .. .	100					
Land and Buildings .. .. .		100				
Lodge (rent less than N.A.V.) .. .. .		120	£120 @ 9/-	54	0	0
		75	£75 @ 9/-	33	15	0
Schedule B—Land .. .. .	£270		(deducted by tenant)			
Vacated under Rule 6 claim .. .. .		Nil.				
Dividends .. .. .		1,540		693	0	0
3½ per cent. War Loan—source discontinued .. .. .		Nil.				
		3,855				
Less Section 34 claim <i>re</i> Agricultural Land ..	300			1,020	0	0
Bank Interest .. .. .	525					
		825				
Statutory Total Income .. .. .		£3,030				
Deduct Allowances—						
Earned Income 1/6th of (£980 ~ £300) ..	113					
Personal .. .. .	180					
Children .. .. .	120					
		413				
Taxable Income .. .. .		£2,617				
Tax payable £50 @ 3/- .. .. .			£7 10 0			
£75 @ 6/- .. .. .			22 10 0			
£2,492 @ 9/- .. .. .			1,121 8 0			
			1,151 8 0			
Less Life Assurance Relief (limited to 1/6th of £3,030),						
£505 @ 7/- .. .. .			176 15 0			
				974	13	0
Refund .. .. .				£645	7	0

\* See Chap. VII, § 2 for basic rules.

## § 3.—Infants and Return of Tax.

Every person acting in any character on behalf of any incapacitated person who cannot be personally charged under the Acts, is required to make such



returns of that incapacitated person's income as may be necessary (§ 101). The term "incapacitated person" includes an infant, whose income is therefore assessed in the hands of the trustee, guardian, etc. (Gen. RR. 4 and 13), but only to the extent that the trustee, etc., has control over the property or income of the infant. There is nothing in the Acts to prevent an infant from being charged in his own name where his property or source of income is under his own control (*R. v. Commissioners of Taxes, ex parte Huxley* (1916), 7 T.C. 49), and in that case he can himself make any claims to which he is entitled, otherwise the person having control of the property, etc., should make the claim.

**(a) Contingent Interest.**

If an infant's interest in property (*under a will or settlement*) is CONTINGENT ON HIS REACHING A CERTAIN AGE OR MARRYING, and the income from the property has to be accumulated in the meanwhile, the trustee can only claim repayment of tax in respect of the child's allowances, to the extent that the income has been expended on the education and maintenance of the infant, and has thereby become vested.

Any balance of income has to be accumulated, and, in the event of the infant's death before the happening of the contingency, would pass with the property to other persons.

The unspent income, therefore, does not vest in the infant until the happening of the contingency, and, if it were not for the special provisions of § 25, 1918, he would not be entitled to any repayment in respect thereof. That section, however, provides that when the contingency occurs, and the income vests, the

child is entitled to claim a repayment of tax for each year during which the income has been accumulating.

The claims that can be made in respect of accumulating income are as follows :—

- (i) Year by year on the amount spent on the child's maintenance and education. Since the payment is made out of net income, the gross equivalent is deemed to be the income of the child for the year, against which tax is repaid on his allowances. This claim must be made within six years from the end of the year of assessment in respect of which it is made.
- (ii) On the happening of the contingency, a claim can be made on the income of each year of accumulation, no matter how long a period it may be, but the claim must be made within six years from the year in which the contingency occurred. Repayment will be made on the child's allowances, less any amounts already repaid under (i).

Any repayment obtained under these provisions is a personal benefit of the claimant, and he is entitled to the whole of it as income (*Fulford v. Hyslop* (1929), 8 A.T.C. 588).

In *Dale v. Mitcalfe* ((1927), 13 T.C. 41), it was held that the beneficiary was entitled to claim under § 25, although the interest in the accumulations was that of a life tenant only.

The only contingencies provided for are the attainment of a specified age and marriage. No claim for

repayment can be made in respect of accumulated income which passes on any other contingency, *e.g.*, where income is to be accumulated for a period (*e.g.*, twenty years from the date of the testator's death) and the capital and accumulations are then to be divided between the surviving children, the benefit of § 25 cannot be claimed (*White v. Whitcher* (1927), 13 T.C. 202).

For the purposes of a repayment claim the income of a beneficiary under a trust is the net amount received (after deduction of the management expenses of the trust) brought up to gross by the addition of the appropriate Income Tax on such gross equivalent (*Murray v. C.I.R.* (1926), 11 T.C. 133; *Macfarlane v. C.I.R.* (1929), 14 T.C. 532).

#### Illustration.

X died on 1st April, 1933, leaving the residue of his estate to accumulate for the benefit of A contingently on A's attaining the age of 21, or marrying under that age. A came of age on 15th May, 1946, having been maintained and educated out of the income. A had no other income.

Year ending 5th April.	Net Income of the Estate.	Amounts applied in maintenance, etc.
1934 ..	£600	£60
1935 ..	620	124
1936 ..	750	155
1937 ..	750	183
1938 ..	750	210
1939 ..	775	232
1940 ..	930	390
1941 ..	915	368
1942 ..	500	340
1943 ..	500	360
1944 ..	500	400
1945 ..	520	400
1946 ..	510	400

The following computations of the claims for 1933-34, 1934-35, 1937-38 and 1941-42 indicate the method to be adopted in computing the claims for all years.

### YEARLY CLAIMS.

	1933-34	1934-35	1937-38	1941-42
Gross Equivalent of sums spent in maintenance	£ 80	Tax 4/6 £ s. d. £36 0 0	£ 280	Tax 10/- £ s. d. £340 0 0
Personal allowance	100	100	100	80
	<u>Nil</u>	<u>£60 (2/3) 6 15 0</u>	<u>£180</u>	<u>£600</u>
			£135 (1/8) 11 5 0	£163 (6/6) 53 12 6
			45 (5/-) 11 5 0	435 (10/-) 217 10 0
			<u>22 10 0</u>	<u>271 2 6</u>
Tax repayable	£20 0 0	<u>£29 5 0</u>	<u>£47 10 0</u>	<u>£68 17 6</u>

### CLAIMS ON COMING OF AGE.

	1933-34	1934-35	1937-38	1941-42
Gross Estate Income	£ 800	Tax £ s. d. 180 0 0	£ 1,000	Tax £ s. d. 500 0 0
Personal allowance	100	100	100	80
	<u>700</u>	<u>900</u>	<u>900</u>	<u>520</u>
	£175 (2/3) 21 17 6	£175 (2/3) 19 13 9	£135 (1/8) 11 5 0	£165 (6/6) 53 12 6
	525 (5/-) 131 5 0	525 (4/6) 118 2 6	765 (5/-) 191 5 0	755 (10/-) 377 10 0
	<u>153 2 6</u>	<u>137 16 3</u>	<u>202 10 0</u>	<u>431 2 6</u>
	46 17 6	42 3 9	47 10 0	68 17 6
	<u>20 0 0</u>	<u>29 5 0</u>	<u>47 10 0</u>	<u>68 17 6</u>
Loss Refund on yearly claim	£26 17 6	<u>£12 13 9</u>	<u>Nil</u>	<u>Nil</u>

Alternatively, the claims for all years can be computed as follows:—  
(P.A. = Personal Allowance; R.R. = Reduced Rate Relief.

Yearly Claim.			On coming of Age.		
Maintenance.	Claim.	£ s. d.	Balance of P.A. R.R.	£ s. d.	£ s. d.
1933—34	P.A. £80 at 5/-	20 0 0	£20 at 5/- £175 at 2/6	5 0 0 21 17 6	26 17 6
1934—35	P.A. 100 at 4/6 R.R. 60 at 2/3	22 10 0 6 15 0			
1935—36	P.A. 100 at 4/6 R.R. 100 at 2/-	22 10 0 15 0 0			
1936—37	P.A. 100 at 4/9 R.R. 135 at 3/2	23 15 0 21 7 6	R.R. £115 at 2/3		12 18 9
1937—38	P.A. 100 at 5/- R.R. 135 at 3/4	25 0 0 22 10 0	R.R. 35 at 3/-		5 5 0
1938—39	P.A. 100 at 5/6 R.R. 135 at 3/10	27 10 0 25 17 6	NH		
1939—40	P.A. 100 at 7/- R.R. 135 at 4/8	35 0 0 31 10 0	NH		
1940—41	P.A. 100 at 8/6 R.R. 165 at 3/6	42 10 0 28 17 6	NH		
1941—42	P.A. 80 at 10/- R.R. 165 at 3/6	40 0 0 28 17 6	NH		
1942—43	P.A. 80 at 10/- R.R. 165 at 3/6	40 0 0 28 17 6	NH		
1943—46	do.	do. each year.	NH	Total ..	£45 1 2

He will claim repayment for 1946-47, in the usual way, as the income has now vested.

**(b) Absolute Interest.**

Where the infant's interest in the property is **ABSOLUTE**, *i.e.*, it is vested immediately, the trustee may claim repayment of tax in the ordinary way on behalf of the infant in respect of the allowances applicable to the gross income from the property each year, irrespective of the amounts expended on maintenance. If, however, the claim is not made year by year, the right to claim may be lost, as it can only be made in respect of the six years preceding the date of the claim (§ 30—1923).

Income arising from a scholarship or similar endowment held by a person receiving full time instruction at a university, college, school, etc., is exempt from Income Tax and Sur-tax (§ 28—1920).

A purchase of shares by a father, registered in the name of his infant child, if made before 22nd April, 1936, is an effective donation of the shares, so as to entitle repayments of Income Tax to be claimed on behalf of the child (*C.I.R. v. Wilson* (1928), 13 T.C. 789). Such a transfer made to-day, however, would not permit a claim to be made as the income would be deemed to be that of the father (*see* Chap. XI, § 4).

**§ 4.—Return of Tax to Charities and other Bodies exempt (§ 37—1918).**

“ ‘Charity’ in its legal sense comprises four principal divisions: trusts for the relief of poverty; trusts for the advancement of education; trusts for the advancement of religion; and trusts for other purposes beneficial to the community not falling under any of the preceding heads ” (*Commissioners for Special Purposes of the Income Tax v. Pemsel* (1891), A.C.

531, *per Lord Macnaghten*). Whether or not any given organisation is a "charity" is a question to be determined on the exact circumstances of the case. Where a trust deed contains purposes other than charitable ones, it is not a trust for charitable purposes only (*Rex v. Special Commissioners, ex parte Rank's Trustees* (1922), 8 T.C. 286).

Charitable institutions are exempt from the payment of Income Tax upon the following income, provided it is applied to charitable purposes:—

- (a) Rents received (Sch. A).
- (b) The annual value of property owned and occupied by the charity, except such part as is in the use and enjoyment of a person whose statutory total income amounts to as much as £150 per annum (§ 30—1921). Annual payments will, of course, be kept in charge so as to account for the tax deducted.
- (c) Interest, annuities and dividends (Sch. C and D).
- (d) The assessable value of lands occupied by the charity (Sch. B), provided the work in connection with the husbandry is mainly carried on by beneficiaries of the charity, and the profits, if any, are applied solely to the purposes of the charity. Such part, however, as is in the use and enjoyment of a person whose statutory total income amounts to as much as £150 per annum is chargeable (§ 30—1921).
- (e) Profits from a trade carried on by the charity (Sch. D), provided the profits are applied solely to the purposes of the charity, and either the trade is exercised in the course

of the actual carrying out of a primary object of the charity, or the work in connection with the trade is mainly carried on by beneficiaries of the charity (§ 30—1921; § 24—1927).

In a case where a charity was entitled to the balance of the profits of a business on which the trustees were assessed under Case I, Schedule D, it was held that this was an annual payment on which the charity was entitled to repayment of Income Tax, the actual receipt being treated as a net figure (*Rex v. Special Commissioners; ex parte Shaftesbury Homes, etc.* (1922), 8 T.C. 367).

Hospitals, almshouses, university colleges and halls, public schools and scientific institutions, are also exempt from tax under Schedule A. In practice, churches are also exempted. The *bond fides* in each case must, however, be satisfactorily proved.

Whether or not a school is entitled to exemption as a public school, under Schedule A, is a question of evidence; the possibility of profit arising to an individual in the course of carrying on a school does not of necessity prevent the school having the character of a public school (*Ereaut v. Girl's Public Day School Trust* (1930), 99 L.J.K.B. 643).

Income assessable under Schedule C may be paid to charities without deduction of tax (Charitable Trusts Amendment Act, 1855, § 28); but in other cases repayment of tax must be claimed from the Special Commissioners.

Similar provisions as to exemption from tax under Schedules A, C and D, apply to a friendly society, which, if unregistered, has not an income in excess of £160 per annum or which, if registered, is precluded by Act of Parliament or by its rules from assuring to any person a sum exceeding £300 by way of a gross sum, or £52 a year by way of annuity. A trade union enjoys a similar exemption to a registered friendly



society in respect of interest and dividends applied solely for the purpose of provident benefits (§ 39).

Savings banks certified under the Trustee Savings Banks Act, 1863, are exempt in respect of their interest and dividends arising from investments with the National Debt Commissioners. The exemption also extends to all income of savings banks which is applied in the payment or credit of interest to any depositor. In any case, however, where the interest paid or credited to any depositor exceeds £15 (§ 24—1924), the bank or branch concerned must make a return to the Inspector of Taxes for the district in which it is situated of the name and address of each such depositor, otherwise it will not obtain the relief to which it is entitled by this section. Any such return must be made before the 1st May in the year following that in respect of which exemption is claimed (§ 39).

National Health Insurance Societies and Committees are exempt in respect of the income from their funds or the investment thereof (§ 39 (5)).

Profits or gains arising to an agricultural society—being a society or institution established for the purpose of promoting the interests of agriculture, horticulture, live stock breeding, or forestry—from an exhibition or show held for the purposes of the society, are exempt from Income Tax, if applied solely to the purposes of the society (§ 23—1924).

## **§ 5.—Co-operative and Similar Societies** (§§ 31-32—1933).

### **(a) Charge of Tax on Mutual Profits.**

Any company or society is liable to tax on its profits under Case I, Sch. D, or Rule 4, Case III (relating to milk-sellers and cattle dealers), whether the profits

arise from dealings with members or with non-members. There is no exemption under any Schedule.

The expression "company or society" means any incorporated company or society whether incorporated in the United Kingdom or elsewhere, and the expression "registered society" means a society registered under the Industrial and Provident Societies Acts, 1893 to 1928, or under the Industrial and Provident Societies Acts (Northern Ireland), 1893 to 1929.

In computing the profits, deductions are allowed for any sums which—

- (a) represent a discount, rebate, dividend, or bonus (commonly known as the "divi.") granted by the company or society to members or other persons in respect of their transactions with the company or society, provided, of course, they are taken into account in the computation; and
- (b) are calculated by reference to the magnitude of the transactions and not by reference to the amount of any share or interest in the capital of the company or society.

A registered society whose business consists mainly in the making of investments, and the principal part of whose income is derived therefrom, is entitled to relief under § 33, 1918, in respect of expenses of management as if it were an investment company. (*See* § 7 of this chapter.)

**(b) Payment of loan and share interest of registered societies without deduction of tax.**

Any share or loan interest paid by a registered society must be paid without deduction of Income Tax unless it is payable to a person whose usual place of abode is not within the United Kingdom.

Interest paid gross is chargeable on the recipient under Case III, Schedule D.

To avoid a double charge, it is provided that the society is entitled to deduct from the tax it would otherwise have to bear for any year of assessment,

a sum representing tax on the amount of interest paid by it in that year without deduction of tax. Where the tax on the interest exceeds the amount of tax which the society would otherwise bear, so that due relief cannot be given for the year of assessment in respect of any part of the interest paid by the society in that year, § 19, 1928, applies as if the society had been assessed under General Rule 21 in respect of the excess interest. The relief does not apply to any loan interest in respect of or by reference to which a deduction or relief is allowable to the society in any other way.

The Special Commissioners will determine disputed claims.

On or before 1st May in each year every registered society must deliver to the Inspector of Taxes for the district in which its registered office is situate a return in the form prescribed by the Commissioners of Inland Revenue showing—

- (a) the name and place of residence of every person to whom loan interest amounting to the sum of five pounds or more has been paid by the society in the year of assessment which ended next before the said 1st May ; and
- (b) the amount of such loan interest paid in that year to each of those persons.

If the return is not duly made, the society is not entitled to any relief in respect of any payments of loan interest which it was required to include in the return, and the amount of any relief or allowance which has been given in respect of any such payments may, if not otherwise made good, be assessed under Case VI of Schedule D.

The expression “share interest,” means any interest, dividend, bonus, or other sum payable to a shareholder of the society by reference to the amount of his holding in the share capital of the society ; and the expression “loan interest” means any interest payable by the society in respect of any mortgage, loan, loan stock, or deposit.

§ 6.—Interest paid to Banks, etc. (§ 36—1918).

Interest paid in the United Kingdom to a banker or a member of the stock exchange or a discount house on advances, is “short” interest, and tax is not deductible at source. It is only right, therefore, that a taxpayer who has to use part of his income in paying such interest, should be entitled to reduce his income by a like amount for Income Tax purposes.

Such interest, if paid in connection with a business, will be charged as an allowable expense in the accounts. If, however, the interest is paid in other circumstances, and the taxpayer can prove that it is paid out of profits or gains brought into charge to tax, he can claim repayment of tax on it (usually by set-off against tax not yet paid), provided the payee is carrying on business in the United Kingdom. Interest paid to an overseas branch of an English bank is “payable in the United Kingdom” as it might lawfully be tendered in England (*Maude v. C.I.R.* (1940), T.R. 139).

The claimant must produce a certificate from the banker or stockbroker, etc., showing the interest paid and the securities held.

Repayment in respect of bank interest can be claimed only by the person to whom the advance was made; not by a guarantor of such advance who has to implement his guarantee (*C.I.R. v. Holder* (1932), 16 T.C. 540).

A claim cannot be made in respect of “contango” interest, or interest paid to moneylenders.

Where interest is allowed as a deduction in the Profit and Loss Account, it is not paid out of profits brought into charge to tax, and no repayment under § 36 is competent; nor is it open to the taxpayer to

reopen the assessments in order to make such a claim (*Muller and Co. v. C.I.R.* (1928), 14 T.C. 116). If the loan is for a capital purpose, the interest is not chargeable in the accounts, and would be the subject of a repayment claim under § 36, unless the interest is in fact capitalised, when no repayment can be claimed (*Metropolitan Railway v. C.I.R.* (1936), W.N. 186).

If the interest is debited to the borrower each half-year and added to the principal of the loan, the interest has not been "paid," and no repayment can be claimed (*Paton v. C.I.R.* (1938), A.C. 341). It is added to the principal of the loan just because it is not paid; repayment can only be claimed in respect of interest paid. Any sums paid in by the borrower to his credit could, however, be appropriated to the interest, and if paid out of his profits or gains brought into charge to tax would enable him to reclaim tax.

#### § 7.—Management Expenses: Insurance Companies, etc. (§ 33—1918).

In the case of life assurance companies, the Crown has the option of charging untaxed interest either under Case I, Schedule D, as part of the profits of the business, or under Cases III, IV or V (as may be appropriate) but not under both (*Norwich Union Fire Insurance Co. v. Magee* (1896), 3 T.C. 457; *Liverpool and London and Globe Insurance Co. v. Bennett* (1913), 6 T.C. 327). Life assurance companies are almost always assessed on an investment basis, however, and, like savings banks, investment companies and similar companies the major part of whose income is derived from investments, are entitled to relief in respect of their management expenses in the year in which the expenses are incurred.

The reason for this will be seen when it is realised that a trading concern pays Income Tax on its *net* profits (*i.e.*, gross profit less allowable expenses), whereas the concerns mentioned above have had all or the major portion of their *gross* profits taxed and, to put them on an equal basis, it is necessary to repay tax on the expenses so as to reduce the tax borne to tax on the *net* profit. The tax repayable is not to exceed the tax suffered by deduction or paid on direct assessments, less the tax recouped from annual payments.

The relief applies to :—

- (a) an assurance company carrying on life assurance business ;
- (b) any company whose business consists mainly in the making of investments and the principal part of whose income is derived therefrom (a company holding real property as an investment comes under this heading, but not a property company holding land for building purposes only) ;
- (c) any savings bank or other bank for savings ;
- (d) a registered society, *i.e.*, one registered under the Industrial and Provident Societies Acts, or under the Industrial and Provident Societies Acts (Northern Ireland), whose business consists mainly in the making of investments, and the principal part of whose income is derived therefrom (§ 31 (4)—1933).

The company or bank claiming must prove to the satisfaction of the Special Commissioners that, for the year of assessment in respect of which the claim is made, it has been charged to tax by deduction or otherwise, and has not been charged under the Rules

of Schedule D, Case I. It is then entitled to repayment of so much of the tax paid by it as is equal to tax on any sums disbursed as expenses of management (including commissions) for that year.

There is the important proviso, however, that the relief given must not make the tax paid by the company or bank less than the tax which would have been paid if all the profits had been charged under Case I.

In arriving at the notional Case I profits for this purpose, all income must be included, even if taxed at source.

The proviso only applies where the company or bank is one that is capable of assessment under Case I; it does not authorise a hypothetical assessment where, as in the case of an investment company, the company is not carrying on a trade and no assessment under Case I is permissible (*Simpson v. Grange Trust* (1935), 19 T.C. 231). The restriction applies to assurance companies, banks, etc., as they are trading and could be assessed under Case I.

The purpose of the proviso is to ensure that a management expenses claim does not place the company in a better position than an ordinary trading concern, *i.e.*, the tax suffered must not be less than that which would have been payable under Case I (on the preceding year's profits).

#### Illustration (1).

An investment company had an income for 1942-43, all taxed at source, of £10,000. Its management expenses amounted to £3,000. The company can claim repayment of tax at 10s. 0d. on £3,000, so that it suffers tax only on its net profit of £7,000.

Had it been a company capable of being assessed under Case I, Schedule D, and its profits for the year to 31st March, 1942, been £8,000, the management expenses claim would have been restricted to tax at 10s. 0d. on £2,000, so as to make the company

suffer tax on £8,000, as this is more than the profit of 1942-43. The excess management expenses could then be carried forward as explained *post*.

Any untaxed interest will be assessed under Cases III, IV and V as usual, but the tax payable is normally set off against the management expenses claim. Where there is any income or profits from sources not charged to tax, such income, etc., is deducted from the management expenses. In the case of an assurance company, the amount of any fines, fees, or profits arising from reversions is deducted from the management expenses for the year. In calculating profits arising from reversions, the company may set off against those profits any loss arising from reversions for any previous year during which any enactment granting this relief was in operation.

Notice of any claim must be given in writing to the Inspector of Taxes within twelve months after the expiration of the year of assessment in respect of which the claim is made. Particulars should be included in the notice. Where the Inspector objects to the claim, the Special Commissioners hear and determine it as an appeal.

The claim may, in practice, be based on the expenses either of the accounting period or of the year of assessment.

A company or bank is not entitled to any relief under this section in respect of any expenses as to which relief may be claimed or allowed under Rules 7 and 8 of No. V of Schedule A, *i.e.*, repairs, maintenance, management and insurance of property.

The following provisions apply to assurance companies only :—

Where an assurance company whose head office is not in the United Kingdom, is charged under Case III on a proportion of the



income from the investments of its assurance fund, or on a substituted basis, the relief is calculated on a like proportion of its total expenses of management for the year.

Where a foreign assurance company carries on business in the United Kingdom, any income of the company from the investments of the life assurance fund (excluding the annuity fund, if any), wherever received, is to be deemed profits under Case III, and the proportion of such income from investments as bears the same ratio to the total income from investments as the amount of premiums received in that year from policy-holders residing in the United Kingdom, or whose proposals were made to the company in the United Kingdom, bears to the total premiums received by the company, is taxable accordingly. Management expenses must be apportioned in the same manner for the purposes of the claim (Case III, R. 3 ; § 33).

Where income arising from the investments of the foreign life assurance fund of an assurance company has been relieved from tax, a corresponding reduction is made in the relief granted in respect of the expenses of management.

Where the profits of life assurance business are computed in accordance with the rules applicable to Case I, there must be excluded such part of those profits as belongs or is allocated to, or is reserved for, or expended on behalf of, policy-holders or annuitants. If, however, any profits so excluded cease at any time to be so reserved and are not allocated to or expended on behalf of policy-holders or annuitants, they are treated as profits for the year in which they are written back from reserve.

Profits arising from the granting of annuities on human life are deducted from the management expenses of a life assurance company, such profits being computed in accordance with the rules applicable to Case I, less losses brought forward on annuity business.

Where an assurance company carries on both ordinary life assurance business and industrial assurance business, the business of each class is treated as though it were a separate business, and § 33, 1918, applies separately to each class.

A mutual assurance company carrying on life assurance business is entitled to relief under § 33, 1918.

In the case of life assurance companies carrying on other classes of insurance, the life assurance business is to be treated as a separate business for Income Tax purposes (Cases I and II, R. 15).

The life assurance profits are determined actuarially, usually every five years, and after deducting any undivided balance from the previous quinquennium, and also the taxed interest during the actual five years, one-fifth of the remaining surplus forms the assessable profit. If a more frequent valuation is taken, the company will be assessed on the average so taken.

A life assurance company is bound to deduct Income Tax from its annuities, and to account for such tax to the Revenue, so far as the annuities are not paid out of profits or gains brought into charge. It cannot treat such annuities as paid out of profits or gains brought into charge to Income Tax to a greater amount than the taxed income of its annuity fund (Gen. R. 21).

For 1940-41 and any subsequent year for which the standard rate exceeds 7/6 in the £, tax borne in respect of income from investments held in connection with life business, to the extent of the excess of (a) the tax borne on that part of the income which belongs to or is allocated to or reserved for, or extended on behalf of policy holders, over (b) the tax which would have been so borne if the standard rate had been 7/6 in the £ is repayable. ("Tax borne" is after allowing any relief for management expenses, etc.) (§ 9 (3)—(No. 2) 1940.)

Where the head office of an assurance company is not in the United Kingdom, the income from investments of the life assurance fund of any branch or agency in the United Kingdom must include all such interest as is mentioned in Rule 2 (d) Sch. C—see Chap. III § 3—or from United Kingdom issues otherwise exempted in the hands of non-residents, and the management expenses relief is to be reduced so as to bear to the relief which would be granted but for the restriction the same proportion as the income excluding interest from Treasury securities bears to the income including such interest (§ 21—1940).

In view of the hardship involved in those cases where the repayment is restricted by reason of the proviso that the repayment is not to reduce the tax borne below the tax which would have been payable if the company had been charged according to the rules of Case I, provision is made for carrying forward the excess expenses (§ 33—1933). The amount of the management expenses on which relief is not granted by reason of the proviso, can be carried forward and treated as management expenses of any of the six following years of assessment. Relief is to be given as soon as possible, *i.e.*, first, in the year next following

the year from which the expenses are carried forward, any balance being carried forward to the next year, and so on, up to the maximum period of six years. Relief for the current year's expenses always comes first, so as to make it quite clear how much of the amount brought forward is used.

It is important to note that an investment company, not being capable of assessment under Case I, cannot carry forward excess management expenses.

#### Illustration (2).

A finance company, capable of assessment under Case I, had the following income and expenses :—

	1943-44	1944-45	1945-46	1946-47
Income taxed at source (gross amount)	£5,000	£6,000	£6,000	£7,000
Dealing profits (assessable Case I)	500	200	900	600
Management expenses	2,000	3,000	3,500	3,000

Show the amounts on which repayment will be made for 1944-45, 1945-46, 1946-47.

#### COMPUTATIONS.

If all profits had been assessable under Case I, the profit for 1943-44 (assessable 1944-45), would have been £5,500 - £2,000 = £3,500, and the succeeding years as follows :—

		1944-45	1945-46	1946-47
Income taxed by deduction ..	..	£6,000	£6,000	£7,000
Dealing Profits .. ..	..	200	900	600
		<hr/>	<hr/>	<hr/>
		6,200	6,900	7,600
Management expenses .. ..	..	3,000	3,500	3,000
		<hr/>	<hr/>	<hr/>
" Adjusted " profit .. ..	..	<u>£3,200</u>	<u>£3,400</u>	<u>£4,600</u>
Preceding year's " adjusted " profit .. ..	..	<u>£3,500</u>	<u>£3,200</u>	<u>£3,400</u>

The management expenses claim must be limited in 1944-45 so as not to reduce the tax borne below the liability based on

the preceding year's profits, but expenses brought forward can be claimed so long as this does not reduce the profits on which tax is borne below the profits of the previous year.

The claims are therefore for repayment of tax on :—

	1944-45	1945-46	1946-47
Current year's expenses .. ..	£2,700*	£3,500	£3,000
Expenses brought forward .. ..	—	200	100
Total .. ..	<u>£2,700</u>	<u>£3,700</u>	<u>£3,100</u>
Amount of expenses carried forward .. ..	<u>£300</u>	<u>£100</u>	
Tax is borne on .. ..	<u>£3,500</u>	<u>£3,200</u>	<u>£4,500</u>

\* £3,000 but restricted to excess of taxed income (£6,200) over previous year's profit (£3,500).

Of the £300 brought forward, only £200 can be the subject of relief in 1945-46 as that reduces the profits on which tax is borne to the profits of the previous year. The other £100 is carried forward to 1946-47.

The following are important matters in making a management expenses claim :—

- (1) As already stated, the accounting year of the business may be adopted as the year of claim in arriving at the expenses and in arriving at the income of the company. Where, however, income is assessable under Cases III, IV or V of Schedule D, the assessments for the year of claim must be substituted for the income from the sources in question.

Alternatively, the claim may proceed on the year of assessment basis, in which case, if the accounting period does not coincide, the relevant figures must be apportioned from the overlapping accounts.

- (2) Only those expenses allowable for Income Tax purposes can be included, and there must be deducted therefrom any income (*e.g.*, transfer fees) which has not been charged to tax by assessment or deduction at source. No relief will be granted in respect of expenses which would be admissible in a maintenance claim under Schedule A (§ 33—1918) even where no such claim has been made (*London and Northern Estates Co. v. Harris* (1937), 3 A.E.R. 252). In practice, however, outlay on the maintenance and repair of premises owned and occupied by the company is allowed as an expense of management, provided it is not included in a maintenance claim under Schedule A.
- (3) Bank interest may be included as an expense instead of being made the subject of a claim under § 36, 1918. The Profits Tax (National Defence Contribution) or Excess Profits Tax is allowed as a management expense (§ 25—1947).
- (4) Where an investment company has raised capital abroad, and pays the interest thereon in local currency, the loss on exchange is not an expense of management (*Bennet v. Underground Electric Railways Co. of London* (1923), 8 T.C. 475).
- (5) Where the company has had Dominion or Double Taxation Tax Relief on part of its income, relief for management expenses is, given first against any income charged at the standard rate, and secondly against any income charged at less than the standard rate.

- (6) Where the company owns and occupies premises, the Net Annual Value cannot be deducted in arriving at the adjusted "profits" for the purposes of the proviso (*i.e.*, where the company could be assessed under Case I), since the Inland Revenue take the view that the charge is off-set by the income (*i.e.*, Net Annual Value), on the other side of the account, it being their view that all income must be included. The Net Annual Value can, however, be included in the management expenses for the year of claim, but the tax thereon must be included in the tax suffered from which a repayment is claimed.
- (7) The Net Annual Value of premises let is allowed as a management expense provided the rents received are brought into credit.
- (8) Brokerage, stamp duties and fees on the change of investments (but not on investment of new capital or undistributed profits) are allowed as management expenses of an investment company up to 1946-47. The position for the future is awaiting decision.

### Illustration (3).

The Revenue Accounts of an investment company for the years ended 31st March, 1946, and 31st March, 1947, are as under:—

	1945-46. £	1946-47. £		1945-46. £	1946-47. £
To Expenses of Administration ..	5,760	6,300	By Dividends, less Tax ..	30,500	28,710
„ Directors' and Auditors' Fees ..	1,750	1,750	„ Interest on Loans, less Tax ..	16,775	20,785
„ Managing Director's Remuneration ..	7,500	7,500	„ Transfer Fees ..	60	50
„ Travelling Expenses ..	1,040	1,830	„ Untaxed Interest (Assessable Case III) ..	300	400
„ Depreciation of Fixtures ..	150	140			
„ Bank Interest ..	3,370	2,860			
„ Income Tax—					
Sch. A on Offices ..	600	540			
Sch. E on Directors' Fees and Managing Director's Remuneration ..	4,870	6,610			
„ Balance, Net Profit ..	22,595	22,365			
	<u>£47,635</u>	<u>£49,895</u>		<u>£47,635</u>	<u>£49,895</u>

(1) Show how the company's Income Tax liability should be dealt with for the year 1946-47.

(2) What effect would it have had if the company was one capable of assessment under Case I.

(1) A claim under § 33, 1918, should be made in writing to the Inspector of Taxes, not later than 5th April, 1948, for a repayment of Income Tax in respect of management expenses, arrived at as follows :—

The management expenses for 1946-47 were :—

Expenses of Administration .. ..	£6,300
Directors' and Auditors' Fees .. ..	1,750
Managing Director's Remuneration ..	7,500
Travelling Expenses .. ..	1,830
Bank Interest .. ..	2,860
Tax on Directors' Fees, etc. .. ..	6,610
Net Annual Value of Offices .. ..	1,200

28,050

*Deduct* : Untaxed Income—Transfer Fees

50

£28,000

Tax deducted from Dividends, 1946-47 ..	£23,490
do. Interest do. ..	16,965
paid under Schedule A .. ..	540

Total Tax suffered on profits, 1946-47 .. 40,995

Tax reclaimed on Management Expenses,

£28,000 at 9/- .. £12,600

*Less* Case III set-off

£300 at 9/- .. 135

12,465

Net tax suffered .. ..

£28,530

The effect is to charge the company on its net profits of the year, viz. :—

Gross dividends .. ..	£52,200
„ interest .. ..	37,700
Transfer fees .. ..	50
Annual Value of premises owned .. ..	1,200
Case III assessment .. ..	300

91,450

*Less* Allowable Expenses .. .. 28,050

Net profit .. .. £63,400

Tax thereon at 9/- .. ..

£28,530

Being a pure investment company, the company cannot be assessed under Case I, and there is no restriction of the claim (*Simpson v. Grange Trust* (1935), 14 A.T.C. 16).

If the adjustment is agreed with the Inspector before the company has paid over the tax on directors' fees, etc., the amount of that tax will be deducted from the tax repayable.

(2) If the company had been capable of being assessed under Case I, the restriction would be computed as follows :—

The adjusted profit of the preceding year (1945-46) was :—

Net Profit per accounts	.. .. .	£22,595
Add—Tax deducted from dividends	..	30,500
do. interest	..	16,775
Sch. A tax	.. .. .	600
Depreciation	.. .. .	150

Profit adjusted in accordance with rules of Case I (treating dividends and interest as part of the trading profits)	.. .. .	<u>£70,620</u>
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Since this exceeds the net profits on which tax has been suffered in 1946-47, the claim will be restricted by the excess, *viz.*, £70,620 - £63,400 = £7,220.

The repayment will then be as follows :—

Tax on management expenses £20,780 at 9/-	..	£9,351
Less Case III assessment (not paid) £300 at 9/-	.. .. .	135
Net repayment	.. .. .	<u>£9,216</u>

The balance of £7,220 expenses can be carried forward.

(As to the special provisions regarding the assessment to Sur-tax of Controlled Investment Companies, see Chap. VIII, § 7 (b).)

The following points affecting insurance companies are included here although they are not connected with management expenses claims :—

In the case of fire and accident insurance companies the usual rule is to carry forward in each year a percentage of the premiums to represent unexpired risks.



In *Imperial Fire Insurance Co. v. Wilson* ((1876), 35 L.T. 271), such a percentage was disallowed on the ground that the adjustment was only made for Income Tax purposes, and the unearned premiums were not actually carried forward in the books.

In *Sun Insurance Office v. Clark* ((1912), A.C. 443), 40 per cent was allowed as deduction by way of unearned premiums. In this case the deduction had actually been made in the books, and the Commissioners had found that it was a reasonable percentage to carry forward. It is a question of facts and figures in each case whether the assessment is fair both to the Crown and to the subject.

### § 8.—Management Expenses ; Royalties, etc.

The lessor of rights to work minerals in the United Kingdom is entitled to claim repayment of the Income Tax paid by him by deduction or otherwise in respect of the rent or royalties on any sums proved to the satisfaction of the Special Commissioners to have been wholly, exclusively, and necessarily disbursed by him as expenses of management or supervision of the minerals in the year of assessment. No repayment of tax will be made on any expenses otherwise allowed as a deduction in computing income for the purposes of Income Tax (§ 26—1922).

The claim must be made within 12 months of the end of the year of assessment, and if the Inspector of Taxes objects to the repayment, the claim is to be heard by the Special Commissioners, and if necessary an appeal may be taken to the Courts on a question of law.

By concession, a similar claim may be made in respect of the following expenses incurred in the management of patent royalties :—

- (a) Revenue expenditure incurred in the United Kingdom by the patent-owner in maintaining his patent in being, *i.e.*, Patent Office

renewal fees, plus agency charges in connection with the renewal.

- (b) Revenue expenditure incurred by the patent-owner under the terms of the contract providing for payment to him of the royalty (*e.g.*, the owner may contract with his licensee to advertise, to adapt the patent to particular circumstances, to provide supervision of an installation, or to report, *etc.*).

The relief is given—so far as expenditure in each year of claim is covered by royalties received in that year—to the owner of the royalties (Report I.T.C.C.).

## CHAPTER X.

**DOUBLE TAXATION and DOMINION  
INCOME TAX RELIEF**

(§§ 51-56—(No. 2) 1945 ; § 27—1920 ; § 46 and  
Fifth Sch., Part II—1927).

**§ 1.—Introduction.**

Income, particularly from businesses and investments, is frequently liable to taxation both in the United Kingdom and in one or more other countries. Within the Empire, a "Dominion Income Tax Relief" has operated for many years, with the aim of taxing the income only at the higher of the two rates involved. It is only recently, with the conclusion of an agreement with the United States of America, that there has been relief in respect of tax suffered in any country outside the British Commonwealth. Following that agreement, similar ones have been made with Canada, Australia, South Africa, Southern Rhodesia, etc., and a somewhat restricted one with France. It is expected that others will follow.

Relief to-day is therefore under one of two heads: (1) Double Taxation Relief where agreements have been concluded ; these give reciprocal exemptions from tax on certain income, and provide for the "foreign" tax being credited against the United Kingdom tax where there is double taxation ; and (2) in other cases on income arising within the Empire, Dominion Income Tax Relief.

Where there is no such relief, the foreign tax is deductible from the income on which it is charged, so

that United Kingdom tax is payable only on the balance ; it will be seen, therefore, that in such a case relief is only given to the extent of United Kingdom tax on the foreign tax paid.

Dominion Income Tax Relief is dealt with first in this Chapter, as it is the older of the two reliefs. It is emphasised that it does not apply where there is in operation a Double Taxation Relief agreement with the country in which the income arises.

Double taxation arises wherever a resident has income taxed here on which he has also paid tax in another country ; it can also arise either where a non-resident is resident in another country and taxable there on United Kingdom income, or where he is in receipt of a dividend from a United Kingdom company paying tax in the other country.

## § 2.—Dominion Income Tax Relief.

In this country, relief is given in full for the tax paid in the Dominion, with the limitation that the relief must not exceed tax on the doubly-taxed income at one-half of the taxpayer's effective rate of tax here. Where the Dominion rate exceeds half the effective British rate, the Dominion should give reciprocal relief, but at the present time such reciprocal relief is not given by all of the Dominions. Where no reciprocal provisions have been made, a special adjustment is necessary, as explained later, whereby the excess of the Dominion tax suffered over the relief given here is allowed to be deducted from the income on which United Kingdom tax is charged.

Special provisions affecting Eire are described later in this Chapter.

(a) *Definition.*

“Dominion Income Tax” is defined as “any Income Tax or Super-tax charged under any law in force in any Dominion, if that tax appears to the Special Commissioners to correspond with United Kingdom Income Tax or Super-tax.” This clearly rules out certain taxes not complying with the conditions; *e.g.*, Federal land tax in Australia, and the railway companies’ tax on miles of permanent way peculiar to some parts of Canada. The term “Dominion” for this purpose includes British Protectorates and countries over which a British mandate is exercised, excluding any country with which there is an agreement for Double Taxation Relief (§ 51 (2)—(No. 2) 1945).

(b) *Persons entitled to relief.*

Relief is granted to any person who has paid, by deduction or otherwise, or is liable to pay, United Kingdom Income Tax for any year of assessment on any part of his income and proves to the satisfaction of the Special Commissioners that he has paid Dominion Income Tax for the same year on the same part of his income. The relief is calculated on the doubly-taxed income at the Dominion rate of tax, or at one-half of the appropriate rate of United Kingdom tax, whichever is the lower.

(c) *Rate.*

The “Dominion rate of tax” is ascertained by dividing the amount of the Dominion Income Tax paid for the year by the amount of the income in respect of which the Dominion Income Tax is charged in the Dominion for that year (before deducting any allowances—other than wear and tear—which the

Dominion laws may provide). This is obviously equitable; the rate must be calculated by reference to the gross figure which will be taxed here. Where, however, the Dominion Income Tax is not charged upon actual ascertained profits, the rate is determined by the Special Commissioners.

### Illustration (1).

A is assessed in a Dominion as follows :—

Profits .. .. .	£1,500
Depreciation .. .. .	300
	<hr/>
	1,200
Abatement .. .. .	£175
Wife's Allowance .. .. .	75
Child's Allowance .. .. .	150
	<hr/>
	400
	<hr/>
	£800 at 5/- = £200.

$$\text{His Dominion rate is } \frac{£200}{1,200} = 3/4$$

The exceptional cases where the determination of the Dominion rate of tax is left to the Special Commissioners, cover instances where the Dominion assessments are on a purely arbitrary basis bearing little or no relation to profits earned in the Dominion, and frequently differing therefrom considerably. To grant relief on the Dominion profits charged to British Income Tax, having regard to the arbitrary rate of tax charged under the Dominion assessment, would not answer in practice, it being apparent that the results might be inequitable either to the Inland Revenue or to the taxpayer.

The “appropriate rate of United Kingdom Income Tax” means the rate at which the claimant has borne, or is liable to bear, United Kingdom Income Tax, to which is added the rate of United Kingdom Sur-tax.

The rate of United Kingdom Income Tax is obtained by dividing the amount of Income Tax payable (before deducting life assurance relief) by the amount of the *taxable* income.

The rate of United Kingdom Sur-tax is obtained by dividing the amount of Sur-tax payable for the *preceding* year by the amount of the *statutory total* income for that preceding year.

In other words, the tax payable is always divided by the amount of income on which it is calculated. The Sur-tax payable in 1947-48 is that for 1946-47, and this must therefore be taken into account, not the Sur-tax for 1947-48, which is not payable until 1948-49.

The appropriate rate for 1947-48 is therefore found by the following formula :—

$$\frac{\text{Income Tax payable for 1947-48}}{\text{Taxable Income for 1947-48}} + \frac{\text{Sur-tax payable in 1947-48 for 1946-47.}}{\text{Statutory Total Income for 1946-47.}}$$

In arriving at the doubly-taxed income, a taxpayer is allowed to utilise his personal and similar allowances to his best advantage, setting them first against non-Dominion income, so as to leave as much as possible available for relief.

#### Illustration (2).

A taxpayer has the following statutory total income for 1947-48 :—

			<i>Tax deducted.</i>		
			£	£	s. d.
Schedule D, Case I assessment	..	..	2,000		
Schedule E do.	..	..	600		
Dividends, etc. (gross amount)	..	..	800	360	0 0
Schedule D, Case IV assessment on income from a Dominion (Dominion rate of tax agreed at 4s. 6d.)	..	..	500		
			3,900		
Less Annual interest	..	..	100	45	0 0
Statutory Total Income	..	..	<u>£3,800</u>	<u>£315</u>	<u>0 0</u>

He is married, with one child under 16, and pays a life assurance premium of £120 on a policy for £3,000 on his own life (policy dated 1930).

His statutory total income for 1946-47 was £4,000.

Calculate the Income Tax payable for 1947-48.

## COMPUTATION, 1947-48.

	£	£	s.	d.
Statutory Total Income, as above .. ..	3,800			
<i>Deduct Allowances—</i>				
Earned Income .. £250				
Personal .. .. 180				
Child .. .. 60				
Sur-tax, 1946-47				
£ s. d.				
£2,000				
500 at 2/- 50 0 0				
500 at 2/6 62 10 0				
1,000 at 3/6 175 0 0				
<u>£4,000</u>	<u>£287 10 0</u>			
		Taxable Income	<u>£3,310</u>	
	£50 at 3/- .. ..			7 10 0
	£75 at 6/- .. ..			22 10 0
	£3,185 at 9/- .. ..			<u>1,433 5 0</u>
				1,463 5 0
		<i>Less Dominion Income Tax</i>		
		Relief (see below)		
		£500 at 4s. 6d.	£112 10 0	
		Life Assurance Relief		
		£120 at 3s. 6d. .. 21 0 0		
				<u>133 10 0</u>
		Tax to be borne .. ..		1,329 15 0
		<i>Deduct tax already suffered</i> .. ..		<u>315 0 0</u>
		Tax still payable .. ..		<u>£1,014 15 0</u>
<i>Dominion Tax Relief :—</i>				
Income Tax Rate	£1,463 5 0	=	8s. 10.1d.	
	<u>3,310</u>			
Sur-tax Rate	£287 10 0	=	1s. 5.25d.	
	<u>4,000</u>			
Effective rate	.. ..		<u>10s. 3.35d.</u>	

Since half the effective rate exceeds the Dominion rate, relief is given at the Dominion Rate of 4s. 6d., *i.e.*, the Dominion Tax paid is allowed as a deduction from the United Kingdom tax.

Had the Dominion rate been 6s. 0d., relief would have been limited to half the effective United Kingdom rate, *i.e.*, £500 at 5s. 1.68d. The Dominion would be expected to give relief in respect of the difference; if it did not do so, an adjustment would arise, as explained later.

Where the income of an individual consists wholly of income from Dominions, the personal and similar



allowances given in arriving at the taxable income have the effect of restricting the Dominion Income Tax relief, as this is allowed only on income doubly taxed, which will be the taxable income, not the whole total income.

### Illustration (3).

A taxpayer has gross income assessed under Case V of £1,008 for 1947-48, derived wholly from a Dominion, and has suffered Dominion tax thereon at the rate of 5s. 6d. He is married, and has two children, in respect of whom deductions are allowed.

			£	s.	d.
Gross Income	..	..	1,008	0	0
Personal Allowance	..	£180			
Children	..	..	120		
			<hr/>	300	0 0
Taxable Income	..	..	<hr/>	£708	0 0
				£	s. d.
Chargeable—					
£50 at 3/-	..	..	..	7	10 0
75 at 6/-	..	..	..	22	10 0
583 at 9/-	..	..	..	262	7 0
				<hr/>	
Gross Tax	..	..	..	292	7 0
Appropriate Rate, $\frac{£292.35}{708} = 8s. 3 1017$					
Less Dominion Income Tax relief :					
£708 at 4s. 1.551d.	..	..	..	146	3 6
				<hr/>	
Net Liability	..	..	..	£146	3 6
				<hr/>	

NOTE.—Since only £708 has been taxed in the United Kingdom only that amount is doubly taxed. Half the effective United Kingdom rate being less than the Dominion rate, relief is restricted accordingly.

The above illustration emphasises the principle that the United Kingdom relief will not go more than half way, *i.e.*, it cannot exceed half the effective United Kingdom rate, which, in this case, gives relief of exactly half the tax payable in the United Kingdom.

(d) *Time at which relief is to be allowed.*

In the case of direct assessments under Cases IV and V, the relief is allowed, if the rates are known in time, in charging the tax.

Where a person has not established his claim before the tax payable is due, however, relief is granted by repayment. The taxpayer must produce the receipts for tax paid in the Dominion, or a certificate in respect of his taxation liability signed by the competent authority in the Dominion, or other means must be found to satisfy the requirements of the Inspector of Taxes. For example, in support of a claim in respect of an Indian dividend, a certificate might be obtained from the secretary of the company, giving details of the effective rates of Indian Income Tax and Super-tax paid on the profits of which the dividend forms a part. The Inspector of Taxes can usually obtain the necessary information through departmental channels, and makes the calculation accordingly. The Indian Income Tax Repayment statement may be required to arrive at the final figures.

(e) *Agreement of Dominion and United Kingdom Incomes.*

The normal basis to be adopted for the purpose of relief is to regard as corresponding to the United Kingdom year of assessment, the Dominion year for which an assessment is made by reference to the same basic period as the United Kingdom assessment on which relief is claimed, *e.g.*, if the Dominion bases its assessment for the year to 31st March, 1946, on the income of the preceding twelve months, this will correspond to 1945-46, which is based on the same period. (This does not, of course, affect dividends

paid direct, *see post*.) The final decision rests with the Commissioners of Inland Revenue to whom the right is reserved to prescribe the Dominion year to be taken as corresponding to the United Kingdom year of assessment.

It is most improbable, owing to the different bases of assessments and rules of computation, that the amounts of the assessments on the same income in the two countries will agree.

So long as the sum taxed in the United Kingdom can be said to be taxed *in toto* in the Dominion by the Dominion assessment, relief can be allowed on the United Kingdom assessment. If, however, certain parts of the income escape Dominion tax altogether, by being excluded from the assessment, there is no double taxation and therefore no relief thereon, *e.g.*, it was decided in the *Assam Railways & Trading Co., Ltd. v C.I.R.* ((1933-34), 18 T.C. 509) that where debenture interest was allowed as a deduction in arriving at the Dominion assessment with the result that the United Kingdom assessment was greater than the Dominion assessment, relief must be restricted to that part of the United Kingdom assessment which in fact referred to doubly-taxed income. In this case, the United Kingdom assessment included debenture interest which was excluded from the Dominion assessment.

It is not necessary, however, to scrutinise the items allowable and disallowable by an individual comparison; nothing need be regarded except the two statutory incomes, taking care to see that neither includes income from any other source. The lower of the two incomes is then the amount on which relief is granted (*C.I.R. v. National Mortgage and Agency Co. of New Zealand* (1938), 2 A.E.R. 88).

*(f) Effect of Losses.*

Owing to the bases of assessment, the position may easily arise that a person has paid Dominion tax in a year in which his United Kingdom assessment on income from that Dominion (based on the previous year) is *nil*. Similarly, he may have to pay United Kingdom tax in a year in which he has no Dominion assessment on the same income. In either case, there is no double taxation and no relief is due (*Rolls Royce, Ltd. v. Short* (1925), 10 T.C. 59). (See § 13.)

A taxpayer who conducts business in more than one Dominion, may make profits in some and losses in others. It is then necessary to determine the amount of profits from each Dominion included in the United Kingdom assessment.

Relief cannot be obtained on an amount in excess of the United Kingdom assessment, but in computing the "make-up" of the assessment, a loss in a Dominion may be set off to the taxpayer's greatest advantage, *i.e.*, used first against those profits chargeable to the highest rates of United Kingdom tax, thus leaving in the assessment the doubly-taxed profits on which relief is obtainable at the highest rates.

*Illustration (1).*

In 1945, a company made a profit, adjusted for Income Tax, of £11,500, which was assessed for the year 1946-47. This result was derived from—

Dominion A	.. Profit	.. ..	£11,000
Dominion B	.. Profit	.. ..	3,000
Dominion C	.. Loss	.. ..	4,000
United Kingdom	Profit	.. ..	1,500

For 1946-47, the Dominion rates were—

Dominion A	.. ..	4s. 0d.
Dominion B	.. ..	2s. 6d.

As there is no profit from Dominion C liable to United Kingdom Income Tax for 1946-47, no relief is due in respect of Dominion C tax.

The assessment will be regarded as made up as follows :—

	Profit.	Deduct Loss, Dominion C.	Make-up of Assessment.
	£	£	£
United Kingdom ..	1,500	1,500	—
Dominion A ..	11,000	—	11,000
Dominion B ..	3,000	2,500	500
	<u>£15,500</u>	<u>£4,000</u>	<u>£11,500</u>

The tax payable for 1946-47 is therefore—

	£	s.	d.	£	s.	d.
£11,500 at 9s. 0d. .. .. .				5,175	0	0
Less Dominion Income Tax Relief—						
Dominion A £11,000 at 4s. 0d. ..	£2,200	0	0			
B     £500 at 2s. 6d. ..	62	10	0			
				<u>2,262</u>	<u>10</u>	<u>0</u>
				<u>£2,912</u>	<u>10</u>	<u>0</u>

The loss in Dominion C is set first against the income arising in the United Kingdom, as this is taxable without relief; the balance of the loss is set against Dominion B income, as this attracts relief only at 2s. 6d., whereas Dominion A income attracts relief at 4s. 0d.

### Illustration (2).

For 1946-47, a company was charged on the previous year's profits of £18,000, being Dominion profits—A £6,000, B £4,000, and United Kingdom profits £8,000. Dominion rates were: A 5s. 3d., B 4s. 0d.

The actual trading for 1946-47 resulted in an adjusted loss of £6,000; Dominion B having made a loss of £9,000, Dominion A a profit of £1,000, and United Kingdom a profit of £2,000. The company claimed relief under § 34.

The loss is regarded as set off as follows :—

	Assessment.	Loss-§ 34.	Net.
	£	£	£
United Kingdom income ..	8,000	2,000	6,000
Dominion A income ..	6,000	—	6,000
Dominion B income ..	4,000	4,000	—
	<u>£18,000</u>	<u>£6,000</u>	<u>£12,000</u>

The loss must obviously be set off first in the Dominion in which it arose, but the balance is set off to the taxpayer's best advantage, *i.e.*, against United Kingdom profits.

Tax payable after § 34 claim—

£12,000 at 9s. 0d.	.. ..	=	£5,400
Less D.I.T.R. £6,000 at *4s. 6d.		=	1,350
			<hr/>
			£4,050
			<hr/>

\* Half the effective United Kingdom rate, being less than the Dominion rate of 5s. 3d.

*(g) Income from several Dominions.*

Where a taxpayer has suffered different Dominion taxes on different parts of his income, each source must be segregated, and dealt with independently. If in any instance, the relief has to be restricted, it is not open to the taxpayer to transfer the excess to another part of the income which has borne Dominion tax at a lower rate.

Similar considerations arise where the income from one source has been subject to more than one Dominion tax, in the same Dominion, *e.g.*, where there is a State as well as Dominion Tax. The two Dominion rates are computed separately, and then aggregated in order to arrive at the Dominion rate of tax suffered on that source of income.

Where income is received from more than one Dominion, personal and similar allowances are again granted to the taxpayer's best advantage, being first set against the income subject to the lowest rate of Dominion Income Tax, in order that the taxpayer may get relief from British tax at the highest rates available. If then not wholly used, the balance of the allowance is applied against the next higher rate until the allowances are fully used.

**Illustration.**

A married taxpayer is assessed for 1946-47 as follows :—

Income from Dominion A	£300	(Dominion Rate 3/6)
„ „ Dominion B	200	(Dominion Rate 2/3)
„ „ Dominion C	100	(Dominion Rate 2/0)
Non-Dominion Income	100	
	<u>£700</u>	
Deduct Personal Allowance	180	
	<u>£520</u>	
Taxable Income ..	<u>£520</u>	

The personal allowance of £180 is deemed to be set first against non-Dominion income, the balance being applied against income subject to Dominion income tax at the lowest rate.

		£	s.	d.	
Tax payable	£50 at 3/- .. ..	7	10	0	
	75 at 6/- .. ..	22	10	0	
	395 at 9/- .. ..	177	15	0	
					207 15 0
Appropriate Rate	£207 15s. 0d. ÷ 520 =	7s.	11	885d.	
The relief is therefore—		£	s.	d.	
Dominion C	£20 at 2s. 0d. ..	2	0	0	
„ B	200 at 2s. 3d. ..	22	10	0	
„ A	300 at 3s. 6d. ..	52	10	0	
					77 0 0
	<u>£520</u>				
Net liability ..		<u>£130</u>	<u>15</u>	<u>0</u>	

*(h) Non-residents.*

Relief is claimable by “any person” who suffers the double taxation, *i.e.*, residence is immaterial. A non-resident person’s appropriate rate is thus the standard rate plus his Sur-tax rate, if any, except in the case of a British subject who is not resident in the United Kingdom. The appropriate rate of the latter is found in exactly the same manner as that of a resident. For the purposes of a claim for relief by a British subject, etc., not resident in the United Kingdom (*see* Chap. II, § 23), Dominion Income Tax Relief is to be left out of account in computing (a)

the amount of the Income Tax payable, and (b) the amount which would be payable if the tax were chargeable on the total income (§ 23—1944). This negatives the decision in *Mackillop v. C.I.R.* ((1943), 2 A.E.R. 215), and reinstates Revenue practice.

The above new provision does not take away the rights of the taxpayer to Dominion Income Tax Relief on income liable to tax in the United Kingdom; it merely means that Dominion Income Tax Relief is not a relief to be taken into account in calculating the proportionate tax under § 24.

### Illustration.

A British subject resident abroad was chargeable as follows :—

1947-48—Income liable to tax in the United Kingdom ..	£3,000
Income not liable to tax in the ,, ,, (earned)	1,500
	<u>£4,500</u>

#### Deduct Allowances—

His Income chargeable to tax in the United Kingdom for 1946-47 was £3,000.	Earned Income abroad .. £250
	Personal .. .. 180
	Children .. .. 120
	<u>550</u>

Notional Taxable Income £3,950

#### Sur-tax, 1946-47.

£2,000 .. .. Nil.	£50 at 3s. .. £7 10 0
£500 at 2/- .. £50 0 0	£75 at 6s. .. 22 10 0
£500 at 2/6 .. 62 10 0	£3,825 at 9s. .. 1,721 5 0
<u>£112 10 0</u>	<u>£1,751 5 0</u>

#### Less Life Assurance Relief—

£120 at 3s. 6d. .. ..	21 0 0
	<u>£1,730 5 0</u>

#### Proportion chargeable in United Kingdom,

$$\frac{3,950}{4,500} \times £1,730 \text{ 5s. 0d.} = £1,153 \text{ 10 0}$$

#### Appropriate rate—

$$\frac{£1,751 \text{ 5s. 0d.}}{£3,950} = \text{say } 8\text{s. } 10\frac{1}{2}\text{d.}$$

$$\text{Add Sur-tax rate } \frac{£112 \text{ 10s. 0d.}}{£3,000} = 9 \text{ d.}$$

$$\underline{\underline{9\text{s. } 7\frac{1}{2}\text{d.}}}$$

Carried forward .. £1,153 10 0



Brought forward ..	£1,153 10 0
The United Kingdom income was from a company taxed in a Dominion at 3s. 9d.	
Dominion Tax Relief, $\frac{9}{13\frac{9}{10}} \times £3950$ at 3s. 9d.	493 15 0
	<hr/> 659 15 0
Less Tax deducted at source by company	
£3,000 limited to U.K. Rate at 5s. 3d. ..	787 10 0
Tax Repayable .. .. .	<hr/> £127 15 0

NOTE.—Since the company received relief at 3s. 9d., its net United Kingdom rate is 9/- less  $3/9 = 5/3$ . It will, however, deduct tax from dividend at the full standard rate, although a taxpayer claiming repayment is not entitled to relief at more than the company's net United Kingdom rate (*see post* § 3).

Only £3,950 is actually taxable, and it seems that relief is at present restricted to the fraction of that figure that the income liable in the United Kingdom bears to the total income.

#### (i) *Paying Agents.*

A paying agent through whom Dominion dividends and interest are paid to persons in this country must deduct tax and account for it to the Inspector of Foreign and Colonial Dividends. This is not affected by § 52—(No. 2) 1945, explained below, as that section deals only with dividends to which General Rule 20 applies.

The agent must deduct tax at the standard rate less Dominion Income Tax, if he can ascertain the rate. The relief should be agreed with the Special Commissioners. The total dividend in the hands of the paying agent has already borne Dominion Income Tax, and therefore an appropriate addition must be made to arrive at the true gross dividend on which United Kingdom Income Tax is chargeable. In cases where the paying agent is not able to ascertain the amount of this addition, he arranges to leave the adjustment to be dealt with by the Inland Revenue authorities directly with the actual recipients by means of an assessment under Case VI, Schedule D.

Where this occurs, the paying agent deducts tax at the standard rate on the dividend in his hands.

### Illustration.

In January, 1948, a paying agent in England received from a company in a reciprocating Dominion a dividend of £195 to be paid over to a shareholder in England. He agreed the Dominion Rate of Tax with the Special Commissioners at 3s. 9d. in the £.

The gross equivalent of this dividend is therefore  $\frac{20}{16\frac{2}{3}} \times £195 = £240$ . Accordingly the agent pays the dividend as follows:—

Amount of Dividend declared .. ..	£195 0 0
Less United Kingdom Income Tax at 5s. 3d. in the £ (i.e., Standard rate 9s. 0d. less Dominion rate 3s. 9d.) on the gross amount of the dividend £240 ..	63 0 0
Net Amount .. .. .	<u>£132 0 0</u>

If the agent had been unable to agree the relief, he would have deducted tax at the standard rate:—

Amount of dividend declared .. ..	£195 0 0
Less United Kingdom tax at 9s. 0d.	87 15 0
	<u>£107 5 0</u>

In the first case, the taxpayer arrives at the gross dividend by grossing up at the standard rate, viz.,  $£132 \times \frac{20}{11} = £240$ . In the latter case, he first grosses up at the standard rate, viz.,  $£107 \text{ 5s. 0d.} \times \frac{20}{11} = £195$ , and then by reference to the Dominion rate ultimately agreed, viz.,  $£195 \times \frac{20}{16\frac{2}{3}} = £240$ . The latter addition, £45, the Dominion tax suffered, has not borne United Kingdom tax, and is therefore assessable under Case VI, Schedule D.

If the taxpayer is married and has other taxed income of £660, his computation in the second case is as follows:—

Dominion Income, Gross .. ..	£240 0 0
Other Income .. .. .	660 0 0
	<u>900 0 0</u>
Less Personal Allowance .. ..	180 0 0
Taxable Income.. .. .	<u>£720 0 0</u>

## Chargeable—

£50 at 3s. 0d.	..	..	..	£7	10	0
75 at 6s. 0d.	..	..	..	22	10	0
595 at 9s. 0d.	..	..	..	267	15	0

---

297 15 0
(Appropriate rate £297 15s. 0d. ÷ 720 = 8s. 8<sup>25</sup>d.)

Less Dominion Tax Relief £240 at 3s. 9d.

45	0	0
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Tax to be borne .. .. 252 15 0

## Less Tax deducted at source—

Dominion Income,

£195 at 9s. 0d. = £87 15 0

Other Income, £660

at 9s. 0d. = 297 0 0

---

384 15 0

---

Tax Repayable .. .. £132 0 0

## His claim is made up of—

Personal Allowance £180 at 9s. 0d. .. £81 0 0

Reduced Rate Allowance £50 at 6s. 0d. 15 0 0

75 at 3s. 0d. 11 5 0

---

107 5 0

## Dominion Income Tax Relief—

£240 at 3/9 .. .. = £45 0 0

Less Tax payable thereon

under Case VI, £45 at 9/- 20 5 0

---

24 15 0

---

£132 0 0

Had the agent been able to pass on relief by deducting tax at 6s. 3d., the computation would have been the same down to the "tax to be borne" line. From that point, it would have proceeded as follows :—

			£	s.	d.
Tax to be borne	..	..	252	15	0

## Less tax deducted at source—

Dominion Income £240 at 5s. 3d. £63 0 0

Other Income £660 at 9s. 0d. 297 0 0

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360 0 0

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Tax Repayable .. .. £107 5 0

As will be seen, this is the tax on allowances, Dominion relief having already been passed on.

(j) *Partnerships.*

Particular care is necessary when dealing with the affairs of a partnership, since the firm is assessed on its income, not the individual partners. Dominion Income Tax Relief, however, is an individual claim, so that the *firm* cannot obtain relief; the claims must be made by the individual partners by reference to their respective circumstances. The income of the partnership must therefore be apportioned between the partners in accordance with their rights as already explained. Each partner's share is aggregated with his other income, and his appropriate rate ascertained (including Sur-tax where payable). Relief is then given to him as relevant in respect of any part of his share of the firm's income which has been doubly taxed.

(k) *Effect of Annual Charges.*

Relief is to be given where a person has paid both Dominion and United Kingdom tax on the same income, and it has been decided that "paid" is not limited to "ultimately borne." The claim may be made by reference to the total income on which United Kingdom tax has actually been paid to the Revenue, notwithstanding that annual charges have been paid out of such income and tax recouped thereon (*C.I.R. v. Dalgety & Co.* (1930), 15 T.C. 216).

Nevertheless, relief is rarely given on more than the statutory total income, *i.e.*, after the deduction of charges.

Where the annual charges are allowed as deductions in computing profits in the Dominion, the sum applied in paying such charges is not eligible for relief, as no double taxation has been suffered thereon (*Assam Railways and Trading Co. v. C.I.R.* (1933-34), 18 T.C. 509).

Following the system of computing relief as favourably as possible to the taxpayer, annual charges are treated as paid first out of income not liable to Dominion tax, next against the Dominion income taxed at the lowest Dominion rate, and so on, in order that as much relief as possible can be claimed.

*(l) Concession where no Dominion Tax owing to different basis.*

In any year where a Dominion profit is included in the assessment to United Kingdom Income Tax, but, owing to the Dominion assessment being calculated by reference to a different period (for which there may have been a loss), no Dominion tax is charged for the corresponding Dominion year of assessment, relief may be applied for as a concession, if there is a title in equity. The concessional relief is generally allowed at the minimum flat rate of Dominion tax prevailing for the period or one-half the United Kingdom effective rate, whichever is the lower. Each case is considered on its own merits, and the authorities review the whole position from the first year in which Dominion Income Tax relief was granted in the particular case.

*(m) Preference Dividends.*

The relief that a British company, which has obtained Dominion Income Tax relief, had to pass on the relief to the shareholders, applied to all dividends, and not merely to dividends payable to ordinary shareholders (*Sheldrick v. South African Breweries, Ltd.* (1923), 1 K.B. 173). The effect was that the preference shareholders actually received a higher net dividend than that to which their contract entitled them, to the detriment of the ordinary shareholders.

In the case of dividends from a Dominion company (incorporated and controlled outside the United Kingdom) on preference shares carrying a fixed rate of dividend and no further right to participate in profits, however, the Board of Inland Revenue took the view that no relief was due where the full rate of dividend had been paid, unless there was a special deduction of Dominion Income Tax from the dividends, as to give relief would result in an artificial gross dividend. This applied to a number of Canadian companies. This view still persists and is in accordance with the new position as regards United Kingdom companies.

**Illustration.**

A Dominion company paid in 1944-45 to a shareholder in the United Kingdom the full dividend on his holding of non-participating preference shares, and his bankers deduct tax so that he receives £90, less tax at 10s. 0d. = £45.

If a claim for Dominion Income Tax relief were allowed, on the assumption that the Dominion company's rate was 4s. 0d. in the £, the gross dividend would be  $£90 \times \frac{20}{18} = £112$  10s. 0d., a purely artificial figure, on which United Kingdom tax at 10s. 0d. in the £ would be chargeable; the net benefit being £56 5s. 0d., so that the shareholder would only have borne £33 15s. 0d. British tax, or 7s. 6d. in the £. No relief was therefore given.

*(n) Non-Reciprocating Dominions.*

Some Dominions do not reciprocate by giving relief in respect of United Kingdom Income Tax. In such a case, the Dominion tax may exceed the relief claimable in the United Kingdom. Such excess is deductible from the Dominion income in computing the assessment or charge in this country.

So long as the income is assessable on the basis of the previous year's income, this occasions no difficulty.

**Illustration (1).**

In 1946-47, the income arising from a non-reciprocating Dominion was £500. The Dominion rate was 5s. and the taxpayer's rate of relief, 4s. 6d. The excess 6d. in the £, amounting

to £12 10s. 0d., is deductible from the income, so that the 1947-48 assessment under Case V, based on the previous year's income, is reduced to £487 10s. 0d.

In the early years of assessment under Cases IV and V, and where dividends are paid through an agent who deducts the United Kingdom tax, so that the "actual" income of the year has to be considered, difficulty is encountered in applying this extra relief. The relief due, and consequently the excess Dominion Income Tax, cannot be ascertained exactly unless the taxpayer's taxable income is known, but in arriving at the taxable income the deduction under the above proviso must be considered.

To overcome this difficulty resort is made to approximation. In the first place, a notional effective rate of Income Tax is found by bringing only the *net* Dominion dividend into the computation. The effective rate of Sur-tax can be ascertained exactly, being based on the preceding year's statutory total income.

Instead of deducting from the gross income the difference between the Dominion tax and the United Kingdom relief, approximately the same result is obtained by grossing the net dividend as if tax had been deducted at the rate at which relief is obtainable. The dividend is therefore grossed as if tax had been deducted at half the notional effective rate (Income Tax plus Sur-tax) so found, or at the Dominion rate, if lower. A new effective rate is then ascertained by re-computing the liability, bringing into account the "gross" dividend so found, and relief is given at that rate.

#### Illustration (2).

A single taxpayer had an income for 1944-45 of £480 from taxed dividends (gross amount) and £2,100 from a non-reciprocating Dominion (after deducting Dominion tax at 6s. 0d.). His effective rate of Sur-tax was 8.772d.

## COMPUTATION.

Dominion Income (net) .. ..	£2,100
Other Income .. ..	480

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 £2,580

Personal Allowance .. ..	80
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 £2,500

£165 at 6s. 6d. .. ..	£53 12 6
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2,335 at 10s. 0d. .. ..	1,167 10 0
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 1,221 2 6

Effective Rate—	s. d.
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Sur-tax .. ..	8·772
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Income Tax	$\frac{£1,221 \text{ 2s. 6d.}}{£2,500} = 9 \text{ 9}·228$
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Notional effective rate ..	<u>10 6</u>	Half = 5s. 3d.
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## RE-COMPUTATION.

Dividends, etc. .. ..	£480
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Dominion Income—	
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£2,100 × $\frac{20}{14\text{s. } 9\text{d.}}$ .. ..	2,847
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 £3,327

Personal Allowance .. ..	80
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 £3,247

£165 at 6s. 6d. .. ..	53 12 6
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3,082 at 10s. 0d. .. ..	1,541 0 0
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 1,594 12 6

Effective Rate—	s. d.
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Sur-tax .. ..	8·772
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Income Tax	
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$\frac{£1,594 \text{ 12s. 6d.}}{£3,247} =$	9 9·866
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 10 6·638

D.I.T.R. £2,847 at 5s. 3·319d. ..	751 2 3
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Tax liability .. ..	843 10 3
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Less Deducted at source	
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£480 at 10s. 0d. .. ..	240 0 0
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Tax still payable .. ..	<u>£603 10 3</u>
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Where British tax is deducted from dividends paid by Dominion companies through agents in the United Kingdom, the method of computation is as shown in the following two illustrations.

### Illustration (3).

For the year 1945-46 Mr. James Brown's final appropriate rate of British tax (including Sur-tax) was 11s. 0d.

He received a cheque for £666 13s. 4d. from Neardone Gold Mines, Limited. A copy of the dividend warrant counterfoil is shown below.

The rate of Dominion tax borne by this company was 6s. 0d. in the £ in respect of the whole of its profits.

There is no reciprocal relief in the Dominion.

Calculate the net further Dominion Income Tax relief due to Mr. Brown.

### NEARDONE GOLD MINES, LIMITED.

(Incorporated in the Dominion of Blank.)

1st August, 1945.

Dividend No. 6 of 1s. per share less British Income Tax at the rate of 5s. 0d. per £ on Gross Dividend on 20,000 shares.

Amount of Warrant £666 13s. 4d.	Amount of Dividend d.
	declared per share .. 12
	<i>Less</i> : British Income Tax
	at 5s. 0d. in the £ on
	the Gross Amount of the
	Dividend, viz., 1s. 4d. 4
	<hr/>
	Net Amount .. 8
	<hr/>

We certify that the British Income Tax deducted from this dividend will be paid to the proper Officer for the receipt of tax.

A. PAYER & Co., *London Secretaries.*

NOTE.—Since the paying agents can only pass on relief at half the standard rate, they must ascertain the gross amount of the dividend declared by grossing at that rate, *i.e.*,

The dividend declared is £1,000

The tax is to be deducted on the gross equivalent of  $£1,000 \times \frac{20}{15} = £1,333 \text{ 6s. 8d.}$

£1,333 6s 8d. at 5s. 0d. = £333 6s. 8d., which deducted from £1,000 leaves a net payment of £666 13s. 4d.

Mr. Brown's appropriate rate of tax is 11s. 0d.

Therefore half his appropriate rate of tax is 5s. 6d.

Since the dividend comes from a reciprocating Dominion, the rate at which the net dividend has to be "grossed" up in respect of Dominion tax is not 6s. 0d. (the rate of Dominion tax suffered) but only 5s. 6d., the rate at which relief is obtainable.

Dividend declared .. .. £1,000 0 0

Gross dividend by reference to 5s. 6d., the rate of relief allowable—

$$1,000 \times \frac{20}{14\frac{1}{2}} = £1,379 \ 6 \ 2$$

Dominion Income Tax Relief due, £1,379 6s. 2d. at 5s. 6d. £379 6 2

Already allowed:—

£1,333 6 8	at 5s. 0d. (A) ..	£333 6 8	
Add : 45 19 6	at 10s. 0d. (B) ..	22 19 9	
			356 6 5
<u>£1,379 6 2</u>			

Net Tax repayable .. .. £22 19 9

(A) = Relief already allowed,  $20,000 \times 4d. = £333 \ 6s. \ 8d.$

(B) = Additional amount of dividend which has borne no tax due to revised grossing up.

#### *Alternative Solution.*

One half of Mr. Brown's appropriate rate of British tax is 5s. 6d., which is less than the Dominion rate of tax suffered, viz., 6s. 0d.

He is therefore entitled to Dominion Income Tax relief at 5s. 6d.

Amount of dividend declared (after deduction of

Dominion tax at 6s. 0d.) .. ..	£1,000 0 0
Gross by reference to rate of relief allowable (5s. 6d.)	379 6 2
Gross Dividend ..	<u>£1,379 6 2</u>

His correct liability is—

Gross Dividend, £1,379 6s. 2d. at 10s. 0d. ..	£689 13 1
Less: Dominion Income Tax relief, £1,379 6s. 2d.	
at 5s. 6d. .. ..	379 6 2
Income tax payable ..	<u>310 6 11</u>
Income tax suffered by deduction $20,000 \times 4d.$	
or £1,333 6s. 8d. at 5s. 0d. .. ..	333 6 8
Repayment due .. ..	<u>£22 19 9</u>

### § 3.—Rate of tax deductible from dividends.

A company's effective rate is always the standard rate, so that a company obtains relief at half the standard rate or at the Dominion rate whichever is lower.

(a) *Position until 20th February, 1946* (§ 52—(No. 2) 1945). Up to the above date a company was required to pass on to its members the relief it obtained, by reducing the rate of tax deducted from its dividends.

#### Illustration (1).

A company's total income for 1944-45 was £24,000, including £20,000 from a Dominion. The Dominion rate of tax was 5s. 9d.

	£	s.	d.
Assessment, 1944-45—£24,000 at 10s. 0d.	12,000	0	0
Less Dominion Income Tax Relief £20,000 at 5s.	5,000	0	0
(half standard rate, being less than Dominion rate).			

Net United Kingdom Tax	£7,000	0	0
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The company, having suffered only £7,000 0s. 0d. United Kingdom tax on £24,000, could deduct at  $\frac{7,000}{24,000} = 5s. 10d.$  in the £, viz.—

	s.	d.
Standard Rate	10	0
Less D.I.T.R. $\frac{7,000}{24,000}$	4	2
	<u>5</u>	<u>10</u>

If the shareholder was a Sur-tax payer, his appropriate rate may have exceeded 10s. 0d., with the result that he has had too little relief and could claim an appropriate refund; if it was less than 10s. 0d., he has had too much relief, and the excess would be assessed upon him under Case VI, or adjusted by reducing tax repayable.

Where the profits of a company had suffered tax in more than one Dominion at varying rates, and a shareholder in this country desired to claim the relief to which he was entitled, the dividend was regarded

as having been paid proportionately out of the various parts of the company's profits, so that certain parts of the dividend would not have borne Dominion tax, while other parts would have been liable thereto at widely differing rates. Having ascertained the rate applicable to each part of the dividend, relief was calculated as if each separate part were a distinct dividend to be grossed at the particular rate.

### Illustration (2).

A Ltd. had a total income for assessment in 1944-45 of £15,000, made up of United Kingdom Income £8,000

Dominion A	do.	£3,000
do. B	do.	£4,000

The appropriate rate of Dominion tax was found to be, in A 4s. 0d., in B 6s. 6d.

Since half the appropriate United Kingdom rate is 5s. 0d., relief is due to the company in respect of Dominion A income at 4s. 0d. and Dominion B income at 5s. 0d.

	£	s.	d.
Assessment—£15,000 at 10s. 0d. ..	7,500	0	0

Less Dominion Tax Relief:—

A.—£3,000 at 4s. 0d. ..	£600		
B.— 4,000 at 5s. 0d. ..	1,000		
	<u>1,600</u>	0	0

Net tax suffered .. ..	£5,900	0	0
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The rate of tax to be deducted from dividends is therefore—

$$\frac{£5,900}{£15,000} = 7s. 10\frac{1}{2}d.$$

The company was bound to pass on to its members the relief, i.e.  $\frac{£1,600}{£15,000} = 2s. 1\frac{1}{2}d.$  in the £. This will have been shown on the dividend warrant as:—

United Kingdom rate .. ..	10	0
Less Dominion Tax Relief .. ..	2	1\frac{1}{2}
Rate of Tax deducted .. ..	<u>7</u>	<u>10\frac{1}{2}</u>

Shareholders, whose appropriate rate differed from that of the company, had to ascertain (through the Inspector of Taxes) what proportions of the dividend were available for relief.

*Dividends declared "free of tax."*

When dealing with "tax free" dividends from a British company, which had obtained relief in respect of the payment of Dominion Income Tax, it was necessary to ascertain the reduced rate of tax the company would have deducted from a gross dividend, and "gross" the free of tax dividend by reference to that rate. (This must not be confused with a dividend from a company abroad, paid through a paying agent here; in that case, the net dividend was grossed at the standard rate, if relief had been passed on; or at the standard rate, and the result in turn grossed at the Dominion rate, if relief had not been passed on.)

**Illustration (3).**

A shareholder received a tax-free dividend, £210, from a British company, and ascertained that the company's rate of United Kingdom Income Tax was 6s. 0d., being the standard rate of 10s. 0d., less Dominion Income Tax relief 4s. 0d. in the £.

For the purpose of any statement of total income, the gross dividend was £300, which was ascertained by treating each 14s. 0d. of net dividend as representing £1 of gross dividend, *viz.*,  $£210 \times \frac{20}{14} = £300$ .

*(b) Position after 20th February, 1946 (§ 52—(No. 2) 1945).*

In the case of any dividend, whether preference or ordinary, from which a company is entitled to deduct tax under General Rule 20, where the company has received relief, either by way of a tax credit under a double taxation agreement, or by way of Dominion Income Tax relief, the company must now deduct United Kingdom tax at *full standard rate*. It must, however, notify the shareholders on the dividend voucher, of its net United Kingdom rate, *i.e.*, the net rate of United Kingdom tax borne by the company, after taking the relief into account.

The company's net United Kingdom rate is found as described above, *i.e.*, by dividing the net tax payable by its statutory total income.

Any Dominion Income Tax relief which had not already been passed on at 20th February, 1946, had to be taken into account in computing the net United Kingdom rate on the first practicable occasion after that date. Similarly, with any tax credit for 1945-46 which would have affected a dividend payable on or before 20th February, 1946, if § 52 had applied before that date.

The relief which has to be taken into account by the company includes any relief which has been taken into account in determining the net United Kingdom rate applicable to dividends received by the company.

#### Illustration (1).

##### A. Company's income —

Case I, Schedule D	..	..	£6,000
Case IV, Schedule D	..	..	4,000
Dividends from B. Company	..	..	2,000
			<u>£12,000</u>

The Case IV profits are taxed in a Dominion at 4/- in £.

##### B. Company's net United Kingdom rate is 6/- in £.

A. Company pays United Kingdom Income Tax on £10,000 at 9/-	..	..	£4,500
Less Dominion Income Tax Relief on £4,000 at 4/-	..	800	
			<u>3,700</u>
On Dividends from B. Company £2,000 at 6/-	..	..	600
			<u>£4,300</u>

Net United Kingdom rate of A. Company  $\frac{£4,300}{12,000} = 7s. 2d.$

The following comparisons of the old and new rules show the effect:—

**Illustration (2).**

A company has a statutory income of £10,000, which has suffered Income Tax in a Dominion at 4/- in the £. It therefore claims Dominion Income Tax Relief at that rate, and pays 5/- in the £ here.

Had the old rules continued, the company would have deducted Income Tax at 5/- in the £ when paying its dividends. If all the profits had been distributed, the result would have been as follows:—

Profits (assuming statutory profit the same as actual commercial profit) ..	£10,000
Less Dominion Income Tax suffered	2,000
	<hr/> 8,000
Less United Kingdom Income Tax at 5/- on £10,000 .. .. .	2,500
	<hr/> £5,500
Net profits available .. .. .	<u>£5,500</u>
Gross equivalent .. .. .	£7,333 6 8
Less Income Tax at 5/- .. .. .	1,833 6 8
	<hr/>
Net dividend .. .. .	<u>£5,500 0 0</u>

Under the new rules, the figures would be these:—

Net profits available .. .. .	<u>£5,500</u>
Gross equivalent .. .. .	£10,000
Less Income Tax at 9/- .. .. .	4,500
	<hr/>
Net dividend .. .. .	<u>£5,500</u>

The method of distribution of relief over a company's financial years is shown by the following example:—

**Illustration (3).**

Dividend declared 15th March, 1948, for year ended 31st December, 1947. The relief to be taken into account is that for the financial year 1947, which is therefore one-quarter of the average rate for 1946-47 plus three-quarters of that for 1947-48, *e.g.*,

1946-47 Statutory Income, £60,000 of which £30,000 has been doubly taxed at  $3/4$  in £.

$$\text{Rate of Relief } \frac{£5,000}{60,000} = 1/8 \text{ in } £.$$

1947-48 Statutory Income £75,000, of which £40,000 has been doubly taxed at  $3/9$  in £.

$$\text{Rate of Relief } \frac{£7,500}{75,000} = 2/- \text{ in } £.$$

The rate of relief for the year ended 31st December, 1947, is therefore  $\frac{1}{4}$  of  $1/8$  plus  $\frac{2}{3}$  of  $2/-$  =  $1/11$  in £, and the company's net United Kingdom rate of tax is  $9/- - 1/11 = 7/1$  in £.

The Board of Inland Revenue recommend companies to print a memorandum on dividend vouchers in the following terms :—

“ By reason of double taxation relief, the net United Kingdom rate of tax payable by the company is      s.      d. in the £. Under Section 52 of the Finance (No. 2) Act, 1945, tax is deductible by the company from this dividend at the full standard rate of      s.

d. in the £, but the rate at which any relief or repayment due may be allowed to a shareholder is limited to the net United Kingdom rate.”

In the case of dividends paid “ free of income tax ” or without deduction of tax, the gross amount which is equivalent to the dividend actually paid is to be computed by reference to the full standard rate. In such cases the second sentence in the memorandum referred to above should begin :—

“ Under Section 52 of the Finance (No. 2) Act, 1945, the gross amount which is equivalent to this dividend for income tax purposes is ascertained by reference to the full standard rate of income tax of      s.      d. in the £, but the rate at which any relief or repayment due may be allowed to a shareholder is limited to the net United Kingdom rate.”



Where the memorandum is printed on the back of the dividend counterfoil, the secretary's certificate should be amplified as follows :—

"I hereby certify that income tax on the profits of the company, of which profits this dividend forms a portion, has been or will be duly paid to the proper officer for the receipt of taxes, and that the company's net United Kingdom rate of tax (see overleaf) is        s.        d. in the £."

*(c) The Shareholder's position.*

Prior to the change in the law, a company was obliged to pass on to its shareholders the Dominion Income Tax relief which it had received, by deducting a correspondingly smaller rate of United Kingdom tax from its dividends, and in most cases this closed the matter. There were instances, however, where the passing on of the relief in this way did not give a taxpayer the full relief to which he was entitled, e.g., where the shareholder was a sur-tax payer, half of whose appropriate rate exceeded half the standard rate, and the company had suffered Dominion Income Tax at more than half the standard rate (and had thus received relief at only half the standard rate); or where half the shareholder's appropriate rate was less than the relief passed on. In such cases appropriate adjustments had to be made.

Since 20th February, 1946, companies must deduct tax from dividends at the full standard rate, irrespective of any Dominion Income Tax relief or double taxation relief they may have received. Nevertheless, a shareholder who is entitled to claim allowances or reliefs is treated as having suffered tax on such dividends only at the company's net United Kingdom rate; and if an annual payment has been made by

the shareholder out of any such dividends, an assessment can if necessary be raised on him under General Rule 21, to enable the excess of the tax deducted over tax at the company's net United Kingdom rate to be collected.

### Illustration (1).

A's income for 1947-48 is as follows :—

Salary	.. .. .	£400
Dividend from Company	.. .. .	200
(Tax deducted £90. Company's net United Kingdom rate 7/6 in £).		

House	.. .. .	40
		<hr/> 640

Less E.I.A.	.. .. .	£67
P.A.	.. .. .	180
Four children	.. .. .	240
		<hr/> 487
		<hr/> <u>£153</u>

#### Chargeable—

£50 at 3/-	.. .. .	£7 10 0
75 at 6/-	.. .. .	22 10 0
28 at 9/-	.. .. .	12 12 0
		<hr/> £42 12 0

#### Less D.I.T. Relief £200

at 1/6	.. .. .	£15 0 0
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#### Life Assurance Relief

£10 at 3/6	.. .. .	1 15 0
		<hr/> 16 15 0

Net liability	.. .. .	<u>£25 17 0</u>
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#### Repayment—

Tax on dividend, £200 at 7/6*	.. .. .	£75 0 0
-------------------------------	---------	---------

Less net liability	.. .. .	25 17 0
		<hr/> £49 3 0

\* See over.

Proof—

Untaxed income .. ..	£440			
Less allowances .. ..	487			
	<u>£47</u>	at 9/-	£21	3 0
Balance of allowances .. ..				
Reduced Rate Relief—				
£50 at 6/- .. ..	£15	0 0		
75 at 3/- .. ..	11	5 0		
			26	5 0
Life assurance relief .. ..			1	15 0
			<u>£49</u>	<u>3 0</u>

Notes.—(1) It is obvious that one-half of A's appropriate rate is greater than the Dominion rate of 1/6 in £.

\* (2) Although the company deducted tax from the dividend at 9/- in £, for the purposes of the repayment claim, A is treated as having paid tax at the company's net United Kingdom rate of 7/6 in £.

## Illustration (2).

B's only income is £600, consisting wholly of dividends from a company which had received Dominion Income Tax Relief at 4/6 in £. B pays annual interest of £100.

	Income.	Income Tax.
	£	£ s. d.
Dividends .. ..	600	*135 0 0
Less Annual interest ..	100	45 0 0
	<u>500</u>	<u>90 0 0</u>
Less Personal allowance	180	
	<u>£320</u>	
Chargeable—	£ s. d.	
£50 at 3/- .. ..	7 10 0	
75 at 6/- .. ..	22 10 0	
195 at 9/- .. ..	87 15 0	
	<u>117 15 0</u>	
Less Dominion Income Tax Relief at $\frac{1}{2}$ appropriate rate		
- £117 15 0 = $\frac{s. d.}{3} = \frac{3}{3} \frac{3-156}{3}$		
on £320 .. ..	58 17 6	
	<u>58 17 6</u>	
Repayment due .. ..		<u>£31 2 6</u>

\*The tax deducted by the company would be £600 at  $\frac{9}{10}$  in £ = £270, but only the net United Kingdom rate of  $\frac{4}{6}$  in £ is available for repayment.

Notes.—(1) B recouped tax by deduction on the annual interest at  $\frac{9}{10}$  in £. By deducting the tax so recouped from the  $\frac{4}{6}$  in £, treated as paid on the dividends, the necessity for raising a Rule 21 assessment on the annual interest at the rate by which  $\frac{9}{10}$  in £ exceeds the net United Kingdom rate is obviated.

(2) B's Dominion Tax Relief is limited to half his appropriate rate, which is less than the Dominion rate of tax suffered. The relief is granted only on the taxable income of £320, which is less than the Dominion Income, as only the taxable income has, in fact, suffered double taxation.

#### § 4.—Double Taxation Relief under Agreements (Tax Credits) (§§ 51-56—(No. 2) 1945).

As already explained, provision has now been made for relief from double taxation in respect of any country or territory outside the United Kingdom with which arrangements are made by the Government of the United Kingdom.

The territories to which these provisions apply are specified by Order in Council from time to time, and operate not only within the British Commonwealth, but in respect of the countries named. On any British Dominion entering into such an agreement the existing arrangements will cease.

At the moment of writing, full agreements have been made with the United States of America, Canada, Australia, New Zealand, South Africa, Southern Rhodesia and Transvaal and a partial one with France.

The agreements provide for the exemption of certain types of income in the country where the taxpayer is not resident, *i.e.*, if he is resident in the United Kingdom, he pays on that income only in the United Kingdom. Certain income, however, remains liable

to tax in both countries, and in these cases, a tax credit is given in the one country for the whole or a proportion of the tax suffered in the other country on that income, so that, in total, only the higher of the two taxes is suffered. If subsequent adjustments show that too little tax has been suffered, the difference is collected under Case VI, Schedule D.

The agreements and regulations are too long to reproduce in this book, and readers interested should obtain copies from H.M. Stationery Office.

The amount of the credit to which a taxpayer is entitled is computed by reference to the appropriate rate of United Kingdom tax which he bears, but cannot exceed the amount of the foreign tax paid on the relevant income.

The United Kingdom appropriate rate is ascertained by dividing the tax payable (before deducting life assurance relief) for the year in question by the taxpayer's *total* (not taxable) income for that year. If the claimant is a Sur-tax payer and the particular double taxation agreement provides for credit to be allowed against sur-tax as well as income tax, the rate is the sum of two rates, the first being that which would have been appropriate if the taxpayer had not been liable to Sur-tax, and the second the rate ascertained by dividing the Sur-tax payable by the amount of his total income.

If the taxpayer makes any annual payments, the tax recouped by deduction therefrom must be deducted in computing the tax he bears, for the purpose of the relief. The total credit obtainable for any year cannot, of course, exceed the total United Kingdom tax suffered for that year.

**Illustration (1).**

A taxpayer has a total income for 1946-47 of £5,000 of which £1,000 is subject to double taxation relief. He pays annual charges of £400.

Income Tax		Sur-tax.	
	£	£	£ s. d.
Income .. ..	5,000	2,000	Nil.
Less annual charges ..	400	500 at 2/-	50 0 0
		500 at 2/6	62 10 0
	4,600	1,000 at 3/6	175 0 0
Less E.I.A. ..	£150	600 at 4/6	135 0 0
P.A. ..	180		
2 children	100		
	430	£4,600	£422 10 0
	<u>£4,170</u>		

Chargeable—	£ s. d.
£50 at 3/- .. ..	7 10 0
75 at 6/- .. ..	22 10 0
4,045 at 9/- .. ..	1,820 5 0
	1,850 5 0
Less life assurance allow- ance £200 at 3/6 ..	35 0 0
	<u>£1,815 5 0</u>

Appropriate Rate :—	£1,850 5 0	s. d.
	4,600	= 8 1 (approx.)
	£422 10 0	= 1 10
	4,600	= 9 11

The credit to be allowed in respect of double taxation will be thus, £1,000 at 9/11 = £495 16s. 8d., or the actual amount of the foreign tax paid, whichever is the lower.

In computing the amount of a person's income, where the foreign income is assessable to United Kingdom tax on the basis of the amounts remitted to the United Kingdom, such remittances are deemed to be increased by the amount of the credit for double

taxation relief. If, for example, in the above illustration, the amount of the foreign income remitted to the United Kingdom had been £1,000, and the foreign income tax paid thereon were £400 (this being less than tax at the appropriate rate on the remittance), the foreign income to include in the computation of total income would be £1,400, tax on which at 9/- in £ would be £630. Against this would be credited the £400 double taxation relief, leaving £230 United Kingdom tax to be paid on the foreign income.

If tax on the remittances at the taxpayer's appropriate rate were less than £400, such lower figure would be added to the remittance for the purpose of the computation.

In computing other forms of income, no deduction is allowed for foreign income tax paid, whether in respect of the same or any other income. Where the income includes a dividend, and under the arrangement foreign income tax not chargeable directly or by deduction in respect thereof is to be taken into account in computing any credit to be given in respect of such dividend, the amount of the income is to be increased by the amount of the foreign tax. If the amount of the credit is reduced by reference to the taxpayer's appropriate United Kingdom rate, a corresponding reduction is made in computing the amount of the income. If the income is assessable on a remittance basis, instead of adding to the remittances the amount of the credit given for double taxation relief, the amount of the foreign tax must be added. For this purpose, however, foreign income tax not chargeable directly or by deduction in respect of the dividend is to be left out of account.

*Paying Agents and Dividends from abroad.*

In the case of dividends paid through agents to persons whose addresses are in the United Kingdom, any foreign (this term is used here to include Dominion) tax which is deductible will be withheld on the other side, without enquiring whether the person beneficially entitled to the dividend is a United Kingdom resident. Where United Kingdom tax is deductible from the dividend, the agent must deduct tax on the gross amount of the dividend at the standard rate reduced by the rate of foreign tax withheld.

**Illustration (2).**

1947-48			
United States of America dividend	..	£400	
Less United States of America withholding tax at 15%	.. .. .	60	
			<hr/>
Amount received by agent	.. ..	340	
Deduct United Kingdom tax at (9/- less 3/- =) 6/- on £400	.. .. .	120	
			<hr/>
Net dividend	.. .. .	<u>£220</u>	

The recipient therefore receives the same dividend as if tax were payable on it at the standard rate only.

The gross amount is, of course, the amount received by the agent grossed by reference to the rate of the tax withheld abroad; e.g., £10 received by the agent, where the withholding tax is 15% (i.e., 3/- in the £), is equivalent to £11 15s. 3d. gross, and the agent must deduct from the £10, tax on £11 15s. 3d. at 6/- = £3 10s. 7d. (leaving £6 9s. 5d. net, which is equivalent to £11 15s. 3d. less tax at 9/-<sup>s</sup> thereon, £5 5s. 10d.).

If the person beneficially entitled to the dividend is not resident in the United Kingdom, the United Kingdom paying agent (who does not then deduct United Kingdom tax) must withhold in sterling the difference between the tax withheld and what would



have been withheld in a case not under the agreement (in the case of the United States of America this is an additional 15%), calculated on the gross dividend. The amounts so deducted must be accounted for quarterly (within 15 days after 31st March, 30th June, etc.), to the Commissioners of Inland Revenue for transmission to the other country.

**Illustration (3).**

United States of America dividend	
received by agent .. .. .	£10 0 0
(Gross equivalent £11 15s. 3d.)	
Withhold additional United	
States of America tax at 15%	
on gross .. .. .	1 15 3
	<hr/>
Pay to person entitled to income ..	<u>£8 4 9</u>

*Interest from abroad paid through agents.*

The paying agent must deduct United Kingdom tax at the standard rate from the interest received by him, whether or not the foreign tax has been deducted. Claims for refund must be made to the foreign authorities. A claim can be filed for future exemption, which will secure the release by the withholding agent of any excess tax withheld. Any supplementary payment so made is liable to United Kingdom tax at the standard rate.

**§ 5.—Agreement with Eire.**

As a result of the agreements between the Governments of the United Kingdom (Great Britain and Northern Ireland) and Eire, reciprocal exemption from Income Tax and Sur-tax is given in the case of persons resident in one of the countries and not in the other, and reciprocal relief is given to persons resident in both countries (§ 23—1926 ; § 21—1928).

Broadly speaking, the position is that a person resident in Eire, and not resident in Great Britain and Northern Ireland, is exempted from United Kingdom tax in respect of property situate and profits arising in Great Britain and Northern Ireland. In the same manner, a person who is resident in Great Britain and Northern Ireland and not resident in Eire is exempted from tax in Eire. A person so exempted in one country must include all his income arising in that country in his return for the purposes of taxation in the country in which he is resident.

A person resident in both countries is able to claim relief in both countries on the doubly-taxed income at half the lower of the two effective rates.

In the case of partnerships, following the usual rule, each partner must be treated separately. It may be that one partner is resident in England, another in Eire, and the third in both. In that case, the first is exempt in Eire, the second in Great Britain, and the third is liable in both, but is entitled to relief in both countries.

For the purposes of the agreement a company, no matter in which country it is incorporated, is deemed to be resident only in that country in which its business is managed and controlled.

A conjoint office has been set up to deal with matters arising, and to accept returns with a view to ascertaining the net tax payable.

For the purpose of giving effect to the agreements, the Rules of Cases IV and V, Schedule D, are amended, so that income accruing to a person resident in Great Britain and Northern Ireland from securities and possessions in Eire, is to be assessed as follows (2nd Sch. Part II—1926 ; § 19 (3)—1940) :—

*Securities (Case IV).* On the full amount of the income arising in the year of assessment, *i.e.*, "actual income."

Possessions other than (a) a business carried on by the taxpayer either solely or in partnership or (b) employment or pension (*Case V, Rule 1*). On the full amount arising in the year of assessment, *i.e.*, "actual income." Where land or buildings in Eire are occupied by a person resident in Great Britain or Northern Ireland, the net annual value for Sch. A in Eire, and the Sch. B assessments in Eire are to be taken as the income; but if the property is let, the rent is the appropriate income.

Earned income from (a) and (b) above (*Case V, Rule 2*). On the same basis as that on which the income would have been computed if the income had arisen in Great Britain or Northern Ireland, subject to a deduction on account of any annual interest, etc., payable out of the income to a person not resident in Great Britain or Northern Ireland. In computing the profits of a trade, business, profession or vocation, an amount equal to the amount charged under Case V in respect of land or buildings used for the purpose of the business is allowed as a deduction. Claims must be made to the Commissioners of Inland Revenue. Appeals against their decision may be made to the Special Commissioners within twenty-one days of the notice of the decision being given to the taxpayer.

A paying agent paying to persons in Great Britain and Northern Ireland, dividends, interest, etc., out of the public revenue of Eire or out of or in respect of any stocks, shares, etc., of any company, society, etc., in Eire need not deduct United Kingdom Income Tax, provided he furnishes to the Commissioners of Inland Revenue full details of the interest, dividends, etc., the name and address of each payee, and the amount to which each payee is entitled. The income will then be assessed under Case IV or V, as the case may be.

The rate of relief in the case of persons resident in both countries is one-half of the person's appropriate rate of British Income Tax, or one-half of his appropriate rate of Eireann tax, whichever is the lower..

The appropriate rate of British Income Tax is found by dividing the amount of tax payable for the year (before deducting assurance relief or double taxation relief) by the amount of his *statutory total* income for that year, and adding (if he is also liable to Sur-tax) the rate ascertained by dividing the amount of British Sur-tax payable for the *same* year by the total statutory income for that year.

The appropriate rate of tax in Eire is similarly computed.

In the case of persons paying Sur-tax, although the Sur-tax must be taken into account in calculating the appropriate rate, the relief is given in two parts ; that in respect of Income Tax proper being given against Income Tax proper ; that in respect of Sur-tax being given against Sur-tax.

For 1948-49 onwards, residents in Eire will be in the same position as other persons receiving dividends from companies which have received double taxation relief ; relief under the agreement with Eire from British Income Tax cannot exceed the net United Kingdom rate of the paying company.

In the case of persons resident in both countries, the relief from British Income Tax in respect of any such dividend is not to exceed the said United Kingdom rate plus (where relevant) the rate of Sur-tax (*i.e.*, British Sur-tax payable divided by total income).

For purposes of reference, the Eire rates of tax and allowances are given in Appendix VI.

The Chancellor of the Exchequer stated in Parliament that if persons resident in Eire, and liable to Eireann Income Tax, who join the Armed Forces of the Crown, become resident in the United Kingdom by reason of

their service, they will not be charged to United Kingdom Income Tax on their income if that income would not have been taxable had they not become so resident. Their service pay out of British Funds will, of course, be subject to tax.

#### Illustration (1).

A is a resident in Great Britain only, but has several sources of income in Eire. He pays in Eire ground rent of £40 and mortgage interest of £90.

A is entitled to have his assessments in Eire discharged, and to be repaid the Income Tax deducted from his income taxed at source, but must keep sufficient in charge to cover the tax he deducts from the ground rent and mortgage interest.

The whole of his income arising in Eire, less annual charges paid in Eire, must be entered in his British return and be charged to tax in Great Britain.

#### Illustration (2).

Had the words "Great Britain" and "Eire" been reversed throughout in the above example, it would be equally accurate.

#### Illustration (3).

B, domiciled in Great Britain, but resident both in that country and in Eire, had the following income :—

House property in Dublin, let at £200, assessed in Eire under Schedule A, at £160.

House property in London, let at £400, assessed under Schedule A, at £420 net.

Dividends from English companies £500.

Interest on  $3\frac{1}{2}\%$  War Loan, £1,000.

House in London, occupied under a lease, assessed under Schedule A, at £80, ground rent £20.

Share of profits from sleeping partnership in U.S.A. 1944-45, £1,000, of which £600 was remitted to London.

Director's Fees from English company, year ended 31st March, 1946, £600, tax deducted under P.A.Y.E., £86 2s. 6d.

B is married and pays to English Insurance Companies £40 per annum in life assurance premiums on policies taken out in 1929. He has three children under 16.

## COMPUTATIONS, 1945-46.

	G.B. & N.I.		Eire
Dublin House Property—Rent ..	£200	N.A.V. .. .. .	£160
London House Property—Rent being less than N.A.V. .. ..	400	Rent .. .. .	400
London Dwelling House—N.A.V. ..	£80	N.A.V. .. .. .	£80
Less Ground Rent ..	20	Less Ground Rent ..	20
	60		60
Dividends—Actual Income of Year ..	500	Actual .. .. .	500
War Loan Interest—Preceding Year	1,000	Preceding Year ..	1,000
U.S.A. Firm—Preceding year ..	1,000	Remittances to Eire ..	Nil
Directors' Fees—Preceding Year ..	600	Preceding year .. ..	600
<i>Statutory Total Income</i> ..	<u>3,760</u>		<u>2,720</u>
<i>Deduct Allowances</i>			
Earned Income .. (1 <sup>st</sup> th)	60	(1 <sup>st</sup> th)	120
Personal .. ..	140		220
Three Children .. ..	150		163
	<u>350</u>		<u>503</u>
<i>Taxable Income</i> .. ..	<u>£3,410</u>		<u>£2,217</u>
Chargeable—			
£165 @ 6s. 6d. .. ..	£53 12 6	£100 @ 3s. 9d. ..	£18 15 0
3,245 @ 10s. 0d. .. ..	1,622 10 0	2,117 @ 7s. 6d. ..	793 17 6
	<u>1,670 2 6</u>		<u>812 12 6</u>
Appropriate Rate—			
£1,670 2 6 = 8s. 11d.		£812 12 6 = 5s. 11½d.	
3,760		2,720	
Less Life Assurance Relief:			
£40 @ 3s. 6d. .. ..	7 0 0	£40 @ 3s. 9d. .. ..	7 10 0
	<u>1,669 2 6</u>		<u>805 2 6</u>
Less Double Taxation Relief:			
£2,760 @ 2s. 11½d. ..	411 2 6	£2,720 @ 2s. 11½d. ..	405 3 4
Tax to be borne .. ..	<u>1,258 0 0</u>		<u>309 19 2</u>
Less Tax suffered by deduction:			
Dublin Property .. ..		£160 @ 7s. 6d. .. ..	60 0 0
London do. £400			
Dividends .. 500			
	<u>£900</u>		
Less Ground Rent	20		
	<u>£880</u>		
at 10/0 = 440 0 0			
Sch. E .. 80 2 6	<u>526 2 6</u>		
Tax payable under Schedules A and D .. ..	<u>£731 17 6</u>	Tax payable under Schedule D .. ..	<u>£830 19 2</u>
Sur-tax—			
£2,000 .. ..	Nil.	£1,500	Nil.
500 @ 2/- .. ..	50 0 0	500 @ 6d. .. ..	12 10 0
500 @ 2/3 .. ..	56 5 0	720 @ 1/- .. ..	36 0 0
760 @ 3/3 .. ..	<u>123 10 0</u>		
	<u>229 15 0</u>		<u>48 10 0</u>
Appropriate Rate—			
£229 15 0 = 1s. 2½d.		£48 10 0 = 4½d.	
3,760		2,720	
Less Double taxation Relief—			
£2,760 @ 2½d. .. ..	24 8 9	£2,720 @ 2½d. say ..	24 5 0
Sur-tax payable .. ..	<u>£205 6 3</u>		<u>£24 5 0</u>

## NOTES.

(1) The appropriate rate of relief is half the sum of the rate of Income Tax *plus* the rate of Sur-tax in Eire, since this is less than the British rate. The relief is given in two portions as shown.

(2) The Case V assessments on *rents* should be noted.

(3) Since B is not domiciled in Eire, he pays only on remittances in respect of the U.S.A. firm. Had he been domiciled in Eire he would have been assessed on the income *arising* in the preceding year. The law in Eire does not follow the British in this respect.

(4) The income from U.S.A. is *not* doubly taxed.

### § 6.—Profits from the business of Shipping, etc.

Reference has been made in the early part of this chapter to the deduction allowed in respect of tax paid in a foreign country, but, following the war years of 1914—1918, the high foreign taxes have operated extremely harshly on businesses carrying on operations in two or more countries. Shipping concerns were in a most unenviable position until § 18, 1923, afforded them certain relief in respect of foreign taxation. The agreements already referred to in § 4 of this Chapter supersede the provisions of § 18, 1923, and prevent double taxation of shipping and air transport profits.

The section provided that—

“If His Majesty in Council is pleased to declare—

- (a) that any profits or gains arising from the business of shipping which are chargeable to British Income Tax are also chargeable to Income Tax payable under the law in force in any foreign state ; and
- (b) that arrangements, as specified in the declaration, have been made with the Government of that foreign state with a view to the granting of relief in cases where such profits and gains are chargeable to both British Income Tax and Income Tax payable in the foreign state ;

then, unless and until the declaration is revoked by His Majesty in Council, the arrangements specified therein shall, so far as they relate to the relief to be granted from British Income Tax, have effect as if enacted in this Act, but only if and so long as the arrangements, so far as they relate to the relief to be granted from the

Income Tax in the foreign state, have the effect of law in the foreign state." (This section was extended by § 9, 1931, to include profits from the business of air transport.)

The Government of the United States of America was the first to make reciprocal arrangements complying with the provisions of § 18, 1923, similar relief having been afforded by the Revenue Act, 1921. Accordingly, His Majesty made a declaration in November, 1924, exempting from 1st May, 1923, American citizens and corporations carrying on the business of shipping in this country with American ships. As part of the agreement, the American Government in return exempted British shipping businesses from United States tax in a similar degree. Further declarations followed later with regard to Norway, Sweden, Denmark, Finland, the Netherlands, Germany, Iceland, Greece, Japan, Canada and France in respect of shipping, and with Germany, the Netherlands and France in respect of air transport. Section 31, 1924, extended the scope of these provisions to British Dominions, including British protectorates and mandated territories.

The way was opened by § 17, 1930, for the conclusion of further reciprocal agreements in respect of agencies. This section reads—

17.—(1) Subject to the provisions of this section if His Majesty in Council is pleased to declare—

(a) that any profits or gains arising directly or indirectly to a person resident in any foreign state or in any part of His Majesty's dominions outside the United Kingdom through an agency in the United Kingdom or to a person resident in the United Kingdom through an agency in any foreign state or in any part of His Majesty's dominions outside the United Kingdom are chargeable both to United Kingdom Income Tax and to Income Tax payable under the law in force in that foreign state or that part of His Majesty's dominions; and

(b) that arrangements as specified in the declaration have been made with the Government concerned with a view to the granting of relief from such double taxation,



then, unless and until the declaration is revoked by His Majesty in Council, the arrangements specified therein shall, so far as they relate to the relief to be granted from United Kingdom Income Tax, have effect as if enacted in this Act, but only if and so long as the arrangements, so far as they relate to the relief to be granted from the Income Tax payable in the foreign state or in the part of His Majesty's dominions, have the effect of law in the foreign state or the part of His Majesty's dominions :

Provided that no arrangements made under this section shall exempt from United Kingdom Income Tax any profits or gains which either—

(i) arise from the sale of goods from a stock in the United Kingdom ; or

(ii) accrue to a person resident in the United Kingdom ; or

(iii) accrue to a person not resident in the United Kingdom directly or indirectly through any branch or management in the United Kingdom or through any agency in the United Kingdom where the agent has and habitually exercises a general authority to negotiate and conclude contracts.

(2) Any declaration made by His Majesty in Council under this section shall be laid before the Commons House of Parliament as soon as may be after it is made and, if an address is presented to His Majesty by that House within twenty-one days on which that House has sat next after the declaration is laid before it, praying that the declaration may be revoked, His Majesty in Council may revoke the declaration and the arrangements specified in the declaration shall thereupon cease to have effect, but without prejudice to the validity of anything previously done thereunder or to the making of a new declaration.

(3) The obligation as to secrecy imposed by any enactment with regard to Income Tax shall not prevent the disclosure to any authorised officer of the foreign state or part of His Majesty's dominions mentioned in the declaration of such facts as may be necessary to enable relief to be duly given in accordance with the arrangements specified in the declaration.

(4) In this section the expression " His Majesty's dominions " includes any territory which is under His Majesty's protection or in respect of which a mandate on behalf of the League of Nations has been accepted by His Majesty and is being exercised by the Government of some part of His Majesty's dominions.

Agreements under § 17, 1930, were concluded with Canada, Finland, Greece, the Netherlands, Newfoundland, New Zealand, Norway, Sweden, Switzerland and South Africa in respect of agency profits.

## CHAPTER XI.

## MISCELLANEOUS.

## § 1.—Isolated Profits.

It is impossible to lay down any hard and fast rules as to whether or not isolated profits, including speculation profits, are assessable to Income Tax; each case will be determined according to the particular circumstances. The term “annual profit” is construed by the Courts to mean any profit which belongs to the year of assessment, even though of a non-recurring nature.

To be a profit, however, the receipt must be in the nature of income as distinct from a capital accretion.

An ordinary member of the public who occasionally indulges in Stock Exchange speculation is not expected to include speculation profits in his return, and is not allowed to deduct speculation losses. If, however, his dealings are fairly continuous, he may be regarded as an operator, and assessed accordingly. Whether an operation constitutes the carrying on of a business or an adventure in the nature of trade or simply the realisation of a capital asset is a question which depends on the facts in each case; the authorities (*i.e.*, decided cases) are mere illustrations of the general principle (*Spiers & Son v. Ogden* (1932), 17 T.C. at p. 125).

In the case of an isolated transaction of purchase and resale there is no middle course open; it is either an adventure in the nature of trade and taxable, or else simply a case of sale and resale of property and thus capital (*Leeming v. Jones* (1929), 15 T.C. at p. 354).

Where a partner in a firm of cotton brokers engaged independently in a series of speculations in cotton futures, the Court held that the transactions were real transactions and not mere bets, and, although the Commissioners had found as a fact that the transactions (in the particular case) were not so habitual or systematic as to constitute a trade, the profits were annual profits or gains assessable under Case VI (*Cooper v. Stubbs* (1925), 10 T.C. 29). This case was followed in *Townsend v. Grundy* ((1933) 18 T.C. 140), where a manufacturer of agricultural implements speculated in cotton futures.

It was held in *Pearn v. Miller* ((1927), 11 T.C. 610), followed by *Leeming v. Jones* ((1930), 15 T.C. 333), that the difference between the cost price and the selling price of goods or property can only be taxed if the purchase and sale was a trade or adventure, or concern in the nature of trade. In determining whether the transaction is or is not in the nature of trade, an important factor appears to be whether the subject matter of the purchase gives the purchaser æsthetic enjoyment (as a picture) or potential income (as an investment or land), while he continues to hold it (*See* Lord President's *dictum* in *C.I.R. v. Fraser* (1942), T.R. 225). If there is no such purpose, then a purchase and sale appears *primâ facie* to be in the nature of trade. "When a man deals with a subject such as whisky in bulk in bond, which he has acquired merely for the purposes of resale, and proceeds to effect a resale of the commodity, he engages in my view in trade only and not in the investment of capital funds" (Lord Moncrieff, *ibid*).

"A transaction being in itself a trading transaction is a sufficient answer to the argument that it was an isolated transaction outside the taxpayer's ordinary business" (*obiter dictum* in *Lindsay and Others v. Commissioners of Inland Revenue* (1932), 18 T.C. at p. 56).

Where a company FORMED FOR THE PURPOSE, *inter alia*, of acquiring and reselling mining property, after purchasing and working various property, resold the whole to a second company, receiving payment in fully paid shares in the latter company, it was held that the difference between the purchase price and the value of the shares for which the property was exchanged was a profit assessable to Income Tax (*Californian Copper Syndicate v. Harris* (1904), 5 T.C. 159).

The importance of the exact facts of the case is well evidenced in the case of *Beams v. Weardale Steel, Coal and Coke Co.* ((1938), 21 T.C. 204), where on incorporation a company formed in 1899 to carry on (*inter alia*) the business of steel manufacturers, iron-masters and colliery proprietors, took over certain slag heaps, then worthless, to one of which it made additions. In 1915, the operations in iron and steel ceased, only colliery operations continuing. At no time did the company work the slag or actively seek to dispose of it, but after 1920, it accepted offers by various persons to buy the slag. The General Commissioners held that the company had not carried on any trading activity in slag disposal, and receipts therefrom must be excluded from the company's trading profits and were not assessable. The Court held that there was evidence on which the Commissioners could arrive at their decision and confirmed it.

If a casual receipt can be regarded as remuneration for services rendered, there is a clear case for assessment under Schedule D, Case II or Case VI, or under Schedule E, according to the circumstances, and it is not necessary for there to be any repetition of the transaction in order to establish liability. It should be remembered, however, that whilst Case VI gives to the Commissioners very wide powers of assessment, if a taxpayer suffers a loss in connection with a transaction, which, if it had resulted in a profit would have been liable to assessment under Case VI, he may claim to set off such loss against Case VI profits or

assessments in the same year or within the six succeeding years (§ 27—1927). The loss could not, however, be set off against profits assessed under any other Case or Schedule (*see* Chap. VII, § 5).

Commission received by directors for guaranteeing a bank overdraft of a company (*Ryall v. Hoare, Ryall v. Honeywill*, (1923), 8 T.C. 521 ; 2 K.B. 447), a bonus to a guarantor for guaranteeing a bank overdraft (*Sherwin v. Barnes* (1931), 16 T.C. 278); an isolated underwriting transaction (*Lyons v. Cowcher* (1926), 10 T.C. 438); and a fee for writing memoirs in a newspaper (*Hooley v. Bladon* (1926), 6 A.T.C. 751), have been held to be “annual profits” assessable under Case VI. Likewise, a partner in a firm of solicitors, who, in consideration of his lending or arranging for a loan to a builder of the purchase price of property, received a share in the resulting profit, was held to be liable under Case VI on his profit (*Wilson v. Mannoch* (1937), 3 A.E.R. 120).

On the other hand, a payment to an author of a book for a licence to publish a new edition and for preparing the MS. for the press, he retaining the copyright, is not an income receipt (*Beare v. Carter* (1940), T.R. 331).

The profits arising from the letting of any non-rateable machinery (the value of which is not taken into account in arriving at annual value under Schedule A) is assessable under Case VI (§ 22—1936).

The sale of a gift is not trading (*Williams v. Davies and v. Nesbet* (1945), 1 A.E.R. 304). The purchase of a large number of endowment policies on other people's lives selected to mature over a period of years (in effect bringing in an annual return), was held to be an adventure in the nature of trade and assessable to tax (*Cordy v. Smith Barry* (1946), T.R. 359).

## § 2.—Liquidator's Liability for Income Tax.

If a liquidator distributes the assets of a company without paying any Income Tax due, he renders himself personally liable to pay the tax, since he will be deemed to have misapplied the assets (*In re Watchmakers' Alliance and Ernest Good's Stores, Ltd.* (1905), 5 T.C. 117; *re New Zealand Joint Stock Corporation* (1907), 23 T.L.R. 238).

A liquidator has responsibilities in respect of any Sur-tax payable by the company in respect of undistributed profits, etc., under § 21, 1922, as amended (*see* Chapter VIII, § 7). Where a company has paid Sur-tax on a direction under § 21, 1922, on its going into liquidation, the Sur-tax applicable to each member's share under the direction must be deducted from his share of surplus (*re Alexander Drew & Co.* (1934), 13 A.T.C. 670).

In a winding-up, sums payable to preference shareholders in respect of arrears of dividend are not subject to taxation by deduction or otherwise, being a share in the assets distributed as capital (*re Dominion Tar and Chemical Co.* (1929), 2 Ch. 387).

By the Companies Act, the Crown is a preferential creditor for one year's assessed tax up to the 5th April preceding the commencement of the winding-up or the appointment of a receiver. The assessment may actually be *made after* the 5th April *in respect of* the year up to that date, but will nevertheless be within the preferential class (*Gowers v. Walker* (1929), 15 T.C. 165). By the Bankruptcy Act, a similar preference is given in bankruptcy, 5th April prior to the date of the receiving order being the relevant date. In both cases, where several years' taxes are unpaid, the Crown is entitled to select

the largest year's liability as preferential (*re Cockell, Jackson v. Attorney-General* (1932), 16 T.C. 681). If a liquidator carries on the business, the Income Tax chargeable in respect of the profits so made must be treated as part of the costs payable before the liquidator is entitled to draw his remuneration (*In re Beni-Felkai Mining Co. Ltd.* (1933), 18 T.C. 632).

The Bankruptcy Regulations agreed between the Board of Trade and the Inland Revenue are reproduced in Appendix V.

### § 3.—Income of Clergymen or Ministers of Religion.

A clergyman or a minister of any religious denomination is assessed under Schedule E in respect of profits, fees or emoluments of his profession or vocation, but any sum or sums paid as expenses incurred by him wholly, exclusively, and necessarily in the performance of his duty may be deducted, *e.g.*, the expenses of visiting members of his congregation; expenses of attending church meetings, where such attendance is part of the duty enjoined on him by his superiors; stationery; Communion expenses; and the actual out-of-pocket expenses of providing a *locum tenens* during incapacitating illness (but not during holiday).

He may also claim an allowance in respect of such part of the rent of his house as represents the portion thereof used mainly and substantially for the purpose of his duty or function of office, not exceeding one-fourth (prior to 1944-45 one-eighth), as the Commissioners may allow. Where no rent is paid, he is deemed to pay a rent equal to the net annual value of the house (Gen. R. 2).

Easter offerings are regarded as profits accruing by reason of office, and are assessable to Income Tax under Schedule E when of a voluntary character, because a rector or vicar has as such a right, at least in theory, to have such offerings (*Blakeston v. Cooper* (1909), A.C. 104). When these offerings are of the nature of ecclesiastical dues they are assessable under Schedule D, Case III. Where a curate receives Whitsuntide offerings expressly solicited as a reward for his "devoted and earnest ministry," *i.e.*, in respect of his work done, he is assessable thereon (*Slaney v. Starkey* (1931), 16 T.C. 45).

Where part of the emoluments of office consist of the use of a house during the term of office, and the tax under Schedule A falls upon the minister himself, the net annual value will be treated as earned income (§ 14 (3)).

Moreover, a clergyman or minister of any religious denomination who occupies a dwelling-house rent free by virtue of his office, in such circumstances that the annual value of the house is not to be regarded as part of his income (*i.e.*, the church pays the tax), may give notice to the Inspector, not later than 30th September in any year, requiring the net annual value, less any annual sum payable in respect of such house, *e.g.*, ground rent, to be treated as his earned income. Where occupation commenced after 30th June, the notice must be given before the expiration of three months from the date of the commencement of such occupation (§ 22—1919). In practice, the claim, once made, has effect for all subsequent years until revoked by notice in writing or until the minister ceases to reside in the house.



The claim is optional ; if the taxpayer is liable to Sur-tax it may not be advantageous to have the annual value treated as part of his total income.

#### Illustration.

A clergyman has a rent-free vicarage assessed at £100 net annual value. His earned income is £600, unearned, £2,600. If he claims that the annual value be treated as his income for 1947-48, he will be allowed £17 at 9s. 0d. = £7 13s. 0d., but his Sur-tax will be increased by £100 at 3s. 6d. = £17 10s. 0d. It is therefore advantageous not to claim.

The expenses of removal of a curate from one place to another are not an admissible deduction from the Schedule E assessment (*Freidson v. Glyn-Thomas* (1922), 8 T.C. 302), nor will deduction be permitted for charitable subscriptions, entertaining, books, or rates, heating, etc., of residence.

#### § 4.—Settlements.

In order to prevent the avoidance of tax by means of settling property on infant children and other dependants, the Income Tax Acts have been amended from time to time, until to-day the law on this aspect of taxation is voluminous and complicated. The relevant sections are reproduced in Appendix XI for the benefit of readers who require detailed information. In the text which follows, the law as it stands to-day is outlined briefly for the requirements of student readers.

Subject to certain exceptions, income under the following settlements is deemed for all purposes of Income Tax and Sur-tax to be income of the settlor and not of the beneficiary :—

- (a) Settlements (including transfers of assets) by a parent in favour of an infant child ;
- (b) Revocable settlements ;

- (c) Settlements operative for a period which cannot exceed six years ;
- (d) Settlements of which the income or capital may revert to the settlor (but only to the extent that the income is undistributed).

The term "settlement" includes any disposition, trust, covenant, agreement or arrangement ; in the case of settlements on infant children, it also includes transfer of assets. It does not include settlements under a will.

It is important to remember that the restrictions only apply for Income Tax (including, of course, Sur-tax) purposes ; in all other respects the settlements are not affected by the Income Tax Acts. Where the income of a settlement is treated as that of the settlor, he must pass on to the trustees or beneficiaries any additional relief he may obtain as a result, and can claim from them any additional tax paid.

**(a) Settlements on Infant Children by their Parents.**

The term "child" includes a stepchild, an adopted child or an illegitimate child. Any settlement by a parent on his child entered into before 22nd April, 1936, which had been made irrevocable before that date, is effective for tax purposes, so long as the settlement is for the life of the parent or the child. If, however, the settlement is for any other period, the income is treated as that of the parent who made the settlement.

Any settlement made on or after the 22nd April, 1936, and any revocable settlement, whenever made, is not effective for tax purposes and the income is treated as that of the parent who made the settlement, unless it is an absolute gift, under which the income

accumulates in the hands of trustees as set out in § 21 (3)—1936.

The meaning given to the expression “revocable” is highly technical, as will be seen by reference to the statutory provisions, but in general terms it means that a settlement is revocable if the parent who makes the settlement is able at any time to repossess himself of the property settled, or of the income, even if he can only do so with the consent of someone else.

The rule that the income is to be treated as that of the parent who makes the settlement applies only if at the commencement of the year of assessment the child was an infant and unmarried, unless the settlement is within the provisions applying to settlements in general, dealt with hereunder.

A gift of any asset, including cash, is caught in the net of the legislation (*Hood-Barrs v. C.I.R.* (1946), T.R. 433).

It should be noted that the above restrictions apply only where the person making the settlement is the parent of the infant child. A settlement by a grandparent or other person is not affected, unless there is some reciprocal or other arrangement whereby the funds are really provided by the parent, but the provisions affecting “other settlements” described below are applicable.

**(b) Settlements other than those on Infant Children by their Parents.**

Where the settlement takes the form of a covenant to pay an annual sum, the annuity will not be regarded as an annual charge of the payer nor as income of the payee—

- (i) If the annual sums are payable for a period which cannot exceed six years. A covenant

to pay for "seven years or life whichever shall be the shorter period" is one which *can* exceed six years and is, therefore, outside this restriction.

- (ii) If the covenant is one which can exceed six years but is capable of revocation, even if the consent of some other person is needed for the revocation. If, however, it cannot be revoked within six years, it is effective so long as it is irrevocable.
- (iii) If the annual payment can be stopped on payment of a penalty.
- (iv) If the annual sum is paid to trustees of a settlement or to a company connected with the settlement, and the income of the settlement or company remains undistributed, *i.e.*, has not been either paid to any person in such a form that it is his income, or used to defray expenses properly chargeable.

In cases where the settlement is of capital funds, the income is to be deemed to be that of the settlor and not of the beneficiary—

- (i) Where the income is payable to some one other than the settlor for a period which cannot exceed six years.
- (ii) If the settlement is revocable within six years so that the income may revert to the settlor or his wife (or widow (*Gaunt v. C.I.R.* (1941), 192 L.T. 19)).
- (iii) To the extent that the settlor has an interest in the income.
- (iv) Where the trustees lend money to the settlor or his wife out of the income, the gross

equivalent of the loans are regarded as income of the settlor. Undistributed income of past years is taken into account for this purpose, so that loans will be treated as out of income in so far as they do not exceed the total credit on income account. Where a loan exceeds such income, the balance will be regarded as income of the following year, but not exceeding the income arising in that year, and so on.

Where a settlement is made for valuable and sufficient consideration, the restrictions do not apply, as there is no question of tax avoidance, the settlor having merely exchanged his assets. There are also saving provisions to protect marriage settlements and certain other cases.

If a settlement cannot be revoked for six or more years, but contains provisions which make it revocable thereafter, it is only effective for tax purposes so long as it is irrevocable.

The provisions have effect where there is more than one settlor or disposer (§ 20—1943).

If there is an enforceable covenant, but in any year the full amount due is not paid, only the amount actually paid (grossed up) is allowable as an annual payment for Sur-tax purposes (*Sinclair v. C.I.R.* (1944), T.R. 103).

In the case of a settlement made on or after 10th April, 1946, no deduction of the gross amount is allowable from the settlor's income for *Sur-tax purposes* unless, under the settlement and the events that occur the income is—

(a) payable to an individual for his own use ; or

- (b) applicable for the benefit of an individual or individuals named in the settlement; or
- (c) applicable for the benefit of a child or children of a named individual; or
- (d) income from property of which the settlor has divested himself absolutely.

No deduction will be allowed for Sur-tax purposes under (a), (b) and (c) if the named individual(s) nor under (c) if either the named individual(s) or the child or children in question, are in the service of the settlor or accustomed to act as the solicitor or agent of the settlor (§ 28—1946).

This provision does away with the Sur-tax saving to persons entering into the common form of seven-year covenant in favour of charities and similar bodies. In the case of settlements for the purpose of dependants and other *individuals*, however, the payments are still deductible from the settlor's income for Sur-tax purposes.

#### Illustrations.

(1) A father entered into a bond to pay an annuity to a child of full age for three years. This cannot exceed six years and the father is chargeable on his whole income without any deduction for the annuity, and the annuity is not treated as income of the child (*Gillies v. C.I.R.* (1929), S.C. 131). An annuity for seven years or life, whichever shall be the shorter period, however, would become income of such a child, as the period *can* exceed six years, and the gross amount of the annuity could therefore be deducted in computing the father's total income for the purposes of Sur-tax.

(2) An irrevocable covenant is entered into whereby a taxpayer binds himself to pay a sum of £200 per annum to a hospital or other charity for his life or seven years, whichever shall be the shorter period. The taxpayer pays this sum less tax, and the hospital or charity, being exempt from tax, recovers from the Inland Revenue the Income Tax deducted.

If the covenant was made prior to 10th April, 1946, the £200 may be deducted in arriving at the payee's total income for Sur-tax purposes ; if made after that date payments under the covenant will not be deductible for Sur-tax purposes although the Income Tax position will be unchanged.

(3) A member of a professional body enters into an irrevocable covenant for a term that may exceed six years to pay to the Benevolent Association connected therewith such annual sum as after deduction of Income Tax at the standard rate shall leave the net sum of one guinea. The Benevolent Fund, as a charity, can reclaim the Income Tax on the gross equivalent. For Sur-tax purposes the position would be as in (2). (*See* § 11 *post* as to "free of tax" covenants.)

**§ 5.—Superannuation Funds** (§ 32—1921 ; § 31—1922 ; § 19—1930 ; S.R. & O., No. 1699—1921 ; S.R. & O., No. 638—1931).

In certain circumstances exemption from Income Tax is granted in respect of the income of a superannuation fund, and of sums paid to such fund by an employer or by an employed person.

Section 32, 1921, deals with pension schemes under which contributions of employers and employees are invested to form a fund.

In order to qualify for exemption, the superannuation fund must be approved by the Commissioners of Inland Revenue. Exemption from Income Tax is then allowed in respect of income derived from investments or deposits, and any sum paid by the employer or by an employee by way of contribution towards the fund is an allowable expense of the year in which it is paid. The employer's contribution is charged as an expense in his accounts, and the employee's contribution is deductible from his salary for the purposes of assessment.

No allowance is made in respect of any contribution by an employee which is not an ordinary annual

contribution. (To be an ordinary annual contribution the contribution must be an annual contribution of an amount which is fixed, or is calculated on some definite basis by reference to the earnings, contributions or numbers of the members of the fund.) A contribution by an employer which is not an ordinary annual contribution, must be treated as the Commissioners may direct, either as an expense incurred in the year in which the sum is paid, or as an expense to be spread over such period of years as the Commissioners think proper.

No allowance is made in respect of any payments in respect of which Life Assurance Relief can be given.

An annuity paid out of an approved fund to a person residing in the United Kingdom is charged under Sch. E, under "pay as you earn" rules (§ 2— I.T. (O. & E.), 1944). The assessment is based on the full amount of the annuity arising in the year of assessment.

The Commissioners must not approve any fund unless it is shown to their satisfaction that—

- (a) the fund is *bond fide* established under irrevocable trusts in connection with some trade or undertaking carried on in the United Kingdom by a person residing therein ;
- (b) the fund has for its sole purpose the provision of annuities for all or any of the following persons in the events specified, *i.e.*,
  - (i) for persons employed in the trade or undertaking either on retirement at a specified age or on becoming incapacitated at some earlier age, or



- (ii) for the widows, children or dependants of persons who are or have been so employed, on the death of those persons ;
- (c) the employer is a contributor to the fund ;
- (d) the fund is recognised by both the employer and the employees.

The Commissioners may, if they think fit, and subject to such conditions, if any, as they think proper to attach to the approval, approve a fund, or any part of a fund, notwithstanding—

- (i) that the rules of the fund provide for the return in certain contingencies of contributions paid to the fund ; or
- (ii) if the main purpose of the fund is the provision of such annuities, that such provision is not its sole purpose ; or
- (iii) that the trade or undertaking in connection with which the fund is established is carried on only partly in the United Kingdom and by a person not residing therein.

Application for the approval of any fund or part of a fund must be made by the trustees of the fund in writing before the end of the year of assessment, to the Inspector of Taxes for the district in which the office of the fund is situated or the fund administered. The application must be supported by a copy of the instrument under which the fund is established and two copies of the rules and of the last accounts, and such other information as the Commissioners may reasonably require.

Any subsequent alterations in the rules, constitution, objects or conditions of the fund must be notified forthwith to the Inspector ; in default of such notification, the approval may be deemed to have been withdrawn at the date from which the alteration had effect.

The Commissioners may withdraw their approval on giving notice to the trustees.

The amount of the employer's contribution which may be deducted as an expense, (a) in the case of a trade of a local authority, is such portion of the authority's total contribution as is made in respect of the persons employed in that trade, and (b) in the case of any other employer must not exceed the amount contributed by him in respect of the persons employed by him in the trade on the profits of which he is assessable to United Kingdom Income Tax.

Where contributions (including interest, if any) are repaid to the employer, the trustees must deduct tax at the rate in force for the year in which the repayment is made. Such a repayment forms part of the recipient's statutory total income for that year. The tax so deducted is recoverable from the trustees as a debt due to the Crown.

Where contributions (including interest, if any) are repaid to an employee during his lifetime, or where a lump sum is paid in commutation of or in lieu of an annuity, Income Tax must be paid by the trustees at the rate of one-fourth of the standard rate for the year in which the repayment or payment is made, except in the case of an employee whose employment was carried on abroad, or the widow, child or dependant of such a person, in which case no tax is payable.

#### Illustration.

Standard rate 9/- in £, gross refund £5 0s. 0d.

Gross refund	..	..	..	..	£5	0	0
Income Tax at 2/3 in £ on <i>net</i>	..	..	..	..	9	0	
(i.e., $\frac{2}{3}$ th of net or $\frac{2}{3}$ th of gross)							
Net refund	..	..	..	..	£4	11	0

The Revenue require tax only on the net sum repaid, i.e., the gross refund equals the sum of the corresponding net refund and tax at one-fourth the standard rate on that net amount.

In the case of annuities paid to non-residents, tax must be deducted and accounted for under General

Rule 21, except where the employment was carried on abroad.

The trustees or other persons managing the fund, and an employer who contributes to a fund must, within 14 days of receiving a notice requiring them, furnish to the Inspector—

(a) a return containing such particulars of contributions as the notice may require ;

(b) a return of the name and residence of every annuitant ; the amount of the annuity ; particulars of contributions (and interest thereon, if any) returned to employer or employee, and of sums paid in commutation or in lieu of annuities ;

(c) a copy of the last accounts of the fund and such other information and particulars as the Commissioners may reasonably require.

Details must be included in the Employer's Return (on the P.A.Y.E. card) of Wages and Salaries of the amounts deducted by the employer from the emoluments paid to an employee or paid on his behalf in respect of the employee's contributions to the fund.

The trustees can claim relief from Income Tax in respect of income from investments or deposits of the fund, and any tax for which they are required to account may be set off in the settlement.

Where only part of a fund is approved, it is the practice to treat a corresponding portion of the income as exempt.

If the fund or part of a fund ceases to be an approved fund, the trustees remain liable to account for tax on sums repaid, or paid in commutation of annuities, in so far as the sum so paid is in respect of contributions made before the fund ceased to be an approved fund.

Where, by any public general Act of Parliament, superannuation allowances or gratuities are payable to employees on their retirement or to their legal personal representative on their death, and that Act requires the employee to make contributions towards the expenses of providing the allowances and gratuities, the contributions for any year may be deducted from the assessment for that year.

On the repayment of any such sums to any employee under the authority of any such Act, the person by or through whom the sums are repaid must deduct an amount equal to the total amount of the Income Tax which would have been paid in respect of those sums if they had not been allowed as deductions from the emoluments of the employee. If the sums are repaid with interest thereon, the payer must deduct an amount equal to the total amount of the Income Tax which would have been paid in respect of that interest if it had actually been paid to the employee in the several years in respect of which it is paid.

#### § 6.—War Pensions, Gratuities, etc.

Income from wounds and disability pensions is exempted from Income Tax (including Sur-tax) (§ 16—1919); also allowances to war widows in respect of children (§ 27—1922). No exemption is given in respect of pensions payable to war widows in their own right. Post war credits and gratuities to members of H.M. Forces, civil defence personnel, etc., are also exempted (§ 23—(No. 2) 1945); as are bounties to members of the Forces who extend their service, and ration and messing allowance to the Forces or women serving in the Auxiliary Services (§ 30—1946).

### § 7.—Uncompleted Contracts.

In businesses where uncompleted contracts are a feature of trading, *e.g.*, builders, hire purchase traders, credit drapers, etc., the taxpayer and the Inspector of Taxes do not always see “eye to eye” regarding the method of evaluating the outstanding portions of contracts. Each case must be treated on its own merits, but, in general terms; if the accounting system follows proper principles, there should be little difficulty in convincing the Inspector of the fairness of the method adopted. In hire purchase transactions, the nature of the articles sold normally determines the method of accounting. Any good treatise on Book-keeping and Accounts can be consulted on this point.

The credit drapers have come to an agreement with the Inland Revenue Authorities as to the method of evaluating the outstanding debts. A copy of the agreement can be obtained from the Inspector of Taxes who deals with the case in which any reader may be interested.

It is only where the taxpayer seeks to make a general percentage reserve for uncompleted contracts that serious disputes must inevitably and rightly arise.

### § 8.—Remuneration paid “free of tax.”

Although such arrangements are not now regarded as desirable, and are illegal in the case of directors of companies, under the Companies Act, 1947, there still remain instances where the Articles of Association, resolutions of shareholders, or specific agreements enable the directors to draw their remuneration “free of tax.” Many large corporations have paid the salaries of their staff under a similar agreement.

In such cases, the remuneration liable to tax is the gross sum arrived at by adding to the actual amount paid to the director or employee in the year the amount of tax paid in the same year in respect of his remuneration.

Prior to 1944-45, in the first two or three years, the computation of the tax was somewhat involved, but thereafter it was perfectly straightforward, since tax was payable upon the previous year's remuneration.

For 1944-45 onwards, the assessment is, of course, always on actual remuneration, the tax being deducted under P.A.Y.E. It is therefore necessary to search the Tax Tables on the occasion of each payment to find the gross pay which, less the appropriate tax, will give the net sum due.

The question as to the treatment of allowances is purely one of agreement between employer and employee. In some cases the employer may take the benefit of the allowances, in other cases the employee; whilst sometimes the allowances will be apportioned between them. A scheme commonly adopted has been to treat the individual as a single man, and for the employer to take the benefit of his allowances as such, leaving him the benefit of the tax on any additional allowances to which he may be entitled.

In view of the heavy rates of tax now in force, it is regarded as contrary to public policy that the recipients of tax-free remuneration should escape the increases, and it was enacted by Sections 26 and 27, 1941, in the case of offices, employments, annuities, pensions and stipends taxed under Sch. E, where (a) by a contract—oral or written—made before 3rd September, 1939, and not varied on or after that date (which

variation must be not later than 22nd July, 1941), or (b) by virtue of some provision contained in an enactment passed before that date and not amended on or after it, the emoluments include a payment to or for the benefit of the recipient of the emoluments in respect of his income tax, that the following limitations shall apply:

The amount paid by the employer or other person liable for 1941-42, or any subsequent year, in respect of income tax (*excluding* sur-tax) is not to exceed the amount which would have been payable if the 1938-39 standard rate and allowances had applied to the year of assessment. The sur-tax for 1940-41 onwards is not to exceed the amount which would have been payable had the 1937-38 rates of sur-tax applied to the year of assessment.

The recipient of the income is entitled to the following adjustments of his liability to income tax for 1941-42 and sur-tax for 1940-41: his total emoluments for the purpose of income tax and his total income for sur-tax so far as ascribable to the emoluments, are to be reduced to what they would have been if in his case—

- (a) the 1937-38 sur-tax rates had applied to 1938-39, 1939-40 and 1940-41; and
- (b) the 1938-39 standard rate and allowances had applied to 1939-40 and 1940-41; and
- (c) the rights and liabilities of the parties had been modified accordingly.

For 1944-45 onwards, as a result of assessment on actual under P.A.Y.E., the commission and income tax for the year of assessment, plus sur-tax payable in that year (*i.e.*, the Sur-tax for the preceding year of assessment) will form the assessment for the year.

It is therefore advisable to dispense with all free of tax agreements, as the complication of calculating the notional liability under the 1941 Act, and deducting the difference, is unwieldy. It is not thought of sufficient practical interest to show specimen illustrations.

### § 9.—Alimony.

A husband who pays alimony under a deed of separation, should deduct tax at the standard rate, even if the payments are made weekly. Should he omit to deduct tax from any payment, there is no power to deduct the arrears from future payments (*re Hatch ; Hatch v. Hatch* (1919), 1 Ch. 351). Where the payment is under an order of Court, tax may be deducted unless the order provides otherwise, or the amount is a "small maintenance payment." If no reference to tax appears in the order, tax is deductible (with the exception stated) even if the payments are made weekly (*Clack v. Clack* (1935), 2 K.B. 109). It is no longer the practice of the Divorce Court to order maintenance to be paid "free of tax," and Courts of Summary Jurisdiction follow the new rules (*Wallis v. Wallis* (1941), P. 69).

Tax is not deductible from small maintenance payments, *i.e.*, payments made under an order of Court in the United Kingdom :—

- (a) to or for the benefit of a woman for her maintenance ; or,
- (b) to any person for the benefit of, or for the maintenance or education of, a person under sixteen years of age,

where the amount under (a) does not exceed £2, and under (b) £1 per week. This new rule applies to all



orders made after the passing of the Finance Act, 1944 (13th July, 1944), and to all small maintenance payments falling due after 5th April, 1945, no matter when the order was made. The recipient is chargeable under Case III, Schedule D, on the basis of the amounts due in the year, so far as paid in that or any other year. The payer is entitled to relief in the same way as for bank interest paid. Any Court making or varying an order must notify the Commissioners of Inland Revenue (§ 25—1944).

Except in the case of small maintenance payments, the gross equivalent is an annual charge of the husband, to which General Rules 19 and 21 apply in the usual way, and is taxed income of the wife (*Spilsbury v. Spofforth* (1937), 21 T.C. 247).

Where, however, the order is not for payment free of tax, and the husband fails to deduct tax, either intentionally or otherwise, the Revenue in the past have made a concession whereby the husband is regarded as making an annual payment equal to the sum actually paid plus tax calculated on the amount of the alimony reduced by the balance of personal and similar allowances not obtained by the wife. The balance of the wife's allowances are thus transferred to the husband for this purpose. The concession was given on the facts of each case.

If such a case arises, application should be made to the Inspector of Taxes.

Allowance for the children of the marriage is given to the party, husband or wife, who maintains the child. If both contribute, the allowance is shared. Payment under order of Court, being an annual charge, does not count as maintenance for this purpose.

It appears that if an order is made against a respondent living abroad for payment of "free of tax" maintenance to his former wife living in England, and his income is not subject to British Income Tax, he must remit a sum which, after the payment of Income Tax thereon, gives the sum mentioned in the order (*Shearn v. Shearn* (1930), 46 T.L.R. 652).

Alimony received from abroad is assessable under Case V (*C.I.R. v. Anderström* (1928), 13 T.C. 482).

Where a settlement made in consequence of a divorce provided that the settlor or his personal representatives would pay to his wife's trustees annually "such sum as after deduction of Income Tax at the standard rate for the time being in force and of every other tax on income for the time being in force shall leave a clear sum of £4,000," it was held that the executors of the deceased settlor must provide a sum sufficient to discharge the Income Tax in respect of the annuity and such proportion of the total Sur-tax payable by the annuitant as the sums on which she was from time to time assessed to Sur-tax in respect of the annuity bore to the total income of the annuitant and her second husband for the purpose of Sur-tax (*In re Horlick's Settlement Trusts; Colledge v. Horlick* (1938), 2 A.E.R. 553).

In divorce cases, where the wife is given custody of the children, the Court order commonly directs the husband to pay to the wife (in addition to a sum for her maintenance) specified sums for the maintenance of the children; such sums are income of the wife, not of the children (*Stevens v. Tirard* (1939), 3 A.E.R. 154; *Spencer v. Robson* (1946), T.R. 169). The wife is then the party maintaining the child and can claim the child allowance.

### § 10.—Annuities.

An annuity paid out of a superannuation fund may be assessed under Case VI instead of by deduction at the source, if the Commissioners so direct. An annuity given as a pension is taxed under Schedule E.

Annuities paid by the National Debt Commissioners, the Post Office Savings Bank, and certain bodies which, under arrangement with the Inland Revenue, do not deduct tax, are assessed under Schedule D, Case III.

In other cases, tax is normally deducted at the standard rate, unless the payer arranges with the Inspector of Taxes either not to deduct tax, owing to the recipient's allowances making him exempt from tax, or to deduct at the reduced rate where the taxpayer is liable at that rate only.

An annuity may, however, be merely the return of premiums plus compound interest, *e.g.*, where an educational policy is taken out with an insurance company whereby a father, in return for the premiums previously paid, receives annual payments for his children for a stated number of years, or, in the event of the prior death of the child, the return of the premiums without interest. In such circumstances only the interest is assessable (*Perrin v. Dickson* (1929), 14 T.C. 608).

Similarly, where the purchase price of an undertaking is a fixed sum payable by instalments, Income Tax is chargeable only on that part of the "annuity" which represents interest (*Secretary of State for India v. Scoble* (1903), 4 T.C. 618).

Any so-called "annuity" which is simply a payment of an ascertained capital sum by instalments is not chargeable to tax, but in cases where the annuity is not in respect of such a payment it is normally income of the recipient, even if it is wholly or partly in respect of a return of capital, *e.g.*, where the agreement with an assurance company provides that the return cannot be less than the capital invested, all payments are income receipts (*Sothorn Smith v. Clancy*

(1941), T.R. 529). The capital sum ceased to exist once it was paid for the annuities ; the guarantee only sets an ascertainable period on the payments which were income.

In a case where A owed B money, and bankruptcy proceedings were compromised on terms which included a covenant by A to pay to B two annual payments of £1,000, and thereafter an annual sum of £250 for so long as B lived, it was held that the payments were capital payments—instalments of the capital consideration under the agreement in discharge of a pre-existing debt—and the payments were therefore outside the scope of the Income Tax Acts (*Dott v. Brown* (1935), 15 A.T.C. 147). Annual payments which may vary with profits or depend upon the duration of life may, therefore, yet be capital.

A voluntary payment, *e.g.*, an allowance by a father to a son, is not a permissible deduction in the payer's computation nor is it assessable on the recipient.

In the case of annuities payable under wills, the following points should be noted :—

- (1) Where a person is bequeathed certain income plus such an amount as will reimburse all Sur-tax payable in respect thereof, the gross equivalents of the sums paid in respect of Sur-tax must be regarded as income of the recipient (*Meeking v. C.I.R.* (1920), 7 T.C. 603).
- (2) The sums paid by the trustees on account of Sur-tax on an annuity left free of Income Tax (including Sur-tax) are additional annuities to which the appropriate Income Tax must be added for the purpose of assessment, *i.e.*, the assessment must be based on the gross amount which will produce the net amount of the annuity after paying the Income Tax and Sur-tax thereon (*Lord Michelham's Trustees v. C.I.R., Exors. of Lady M.* v. *C.I.R.* (1930), 15 T.C. 737).

- (3) Where a will provides that an annuity is "free of deductions," this does not include Income Tax, unless the testator indicates that he understands Income Tax to be a deduction (*Turner v. Mullineux* (1861), 1 J. & H. 334). But if the will directs that an annuity is to be paid "free of Income Tax," the trustees must account for the tax thereon. A direction in a will or a codicil that the payment is to be made "clear of all deductions including Income Tax" was held not to include Sur-tax, but merely those deductions for which the trustees are accountable, *i.e.*, the standard rate portion of Income Tax (*In re Crawshay, Crawshay v. Crawshay* (1915), W.N. 412).
- (4) Unless the contract denotes otherwise, the term "free of all taxes (including income tax) and duties" refers only to United Kingdom taxes and duties (*In re Frazer* (1941), T.R. 91). This might be different where the beneficiary was resident abroad.

A direction that an annuity be paid "free of all deductions including Income Tax and Government duty" does not extend to Sur-tax, since Sur-tax is not a tax the burden of which can fall upon the estate and be passed on by deduction (*Prentice's Trustees v. Prentice* (1934), 13 A.T.C. 612). A direction under a will that an annuitant was to be paid out of income "a clear yearly sum after paying or deducting Income Tax and Super-tax," was held to include the proportion of Sur-tax payable in respect of the annuity (*In re Hulton, Hulton v. Midland Bank Executor and Trustee Co.* (1930), 99 L.J. Ch. 316).

In his judgment, Bennett, J., said "If the testator had simply directed his trustees to pay to his wife out of the income of his trust estate such an amount as would give her a clear yearly sum of £12,000 after paying or deducting Income Tax it would, I think, have been reasonably clear that the trustees would have been bound to pay not only the Income Tax at what is now known as the standard rate, but also the Sur-tax attracted by an annuity given in such a form; see *in re Crosse* ((1920), 1 Ch. 240). But the limitation as regards Income Tax contained in the clause will, so long as Sur-tax continues to be charged at the rates now in force, throw upon the annuitant the burden of discharging a considerable part of the Sur-tax attracted by an annuity unless what is in effect a direction to the trustees to pay the Sur-tax attracted by the annuity out of the income of the trust estate can be construed as a direction to pay the Sur-tax . . . . . As far as I can see there is no real or substantial difference between Super-tax and Sur-tax . . . . . In every essential feature Super-tax and Sur-tax are, in my judgment, the same tax."

Where a beneficiary under a trust had a separate income of less than £2,000 per annum, and an annuity under the trust of £4,000 free of Income Tax and Sur-tax, it was held that the trustees must pay out of the residue of the estate such proportion of the total Sur-tax payable by the beneficiary, as the £4,000 annuity with Income Tax added bore to the total amount of the Sur-tax assessment (*Wimble v. Bowring* (1918), 34 T.L.R. 575).

Where an annuity is payable "free of Income Tax," an annuitant obtaining any repayment of tax is required by the trustees under the will or settlement to hand over to them such a proportion of the repayment as the annuity bears to the total income of the annuitant. That proportion forms part of the residuary estate of the trust (*re Pettit; Le Fevre v. Pettit* (1922), 2 Ch. 765). Were it not for this rule the annuitant would in the end have received out of the estate more than 20s. in the £ on the gift.

In practice, the proportion of the refund is not handed over to the trustees, but is deducted by them from the next instalment of the annuity. The annuitant is a trustee of his statutory right to recover for the benefit of the estate Income Tax overpaid in respect of the annuity and is bound at the request of the trustees to sign the proper claim form (*In re Kingcombe; Hickley v. Kingcombe* (1936), Ch. 566).

Where there is untaxed income, it would appear from *re Pettit (supra)* that only the proportion of the Income Tax recovered is to be accounted for to the estate, but this appears to conflict with the decision in *re Day; Public Trustee v. Day* ((1922), Ch. unreported) from which it seems that the annuitant should account for the proportion of Income Tax on his or her allowances.

(See §11 *post* as to the present modifications of free of tax payments.)

It has also been held that the *Pettit* rule applies to an annuity of such an annual sum as will "after deduction of Income Tax but not Sur-tax, leave in her hands the sum of £x clear of all deductions for Income Tax but not Sur-tax." This means £x clear of deduction of Income Tax computed in relation to the annuitant's reliefs and allowances (*re MacLennan, Few v. Byrne* (1939), 3 A.E.R. 81).

In Scotland, the position is different; in *Richmond's Trustees v. Richmond* ((1935), 14 A.T.C. 489), the Court of Session held that the trustees were not entitled to recover any part of the personal allowances from the annuitant, nor to take them into account by way of deduction from the amount of the annuity, in so far as the allowances were covered by her personal income.

Where an annuity was given "clear of all death duties and income tax up to but not exceeding 5/6 in the pound but not sur-tax," it was held that the principle of *In re Pettit* applied, and the annuitant was liable to pay over to the trustees part of any sums received in respect of allowances and reliefs in the proportion in which the whole tax had been borne by the annuitant and by the estate respectively. Moreover, the post-war credits should be accounted for by the annuitant to the trustees in the same proportion (*In re Bates* (1945), T.R. 369). Similarly in *In re Arno* ((1947), T.R. 41), where the annuity was given "without deduction of Income Tax up to a maximum of 5/- in the £," it was held that the direction as to partial freedom from tax was not intended merely for the purpose of ascertaining the gross amounts of the annuities, and the annuitant was obliged to account to the trustees for the amounts of any reliefs.

If the will directs that the annuity is such as, "after deduction of Income Tax therefrom at the current rate for the time being, will amount to the clear yearly sum of £x," this is not equivalent to a "free of tax" annuity, but is a fluctuating annuity, measured by a constant net sum, and the annuitant can retain any Income Tax recovered (*re Jones, Jones v. Jones* (1933), W.N. 176).

If annuitants under a will have made up out of capital deficiencies in income, the amounts paid out of capital are nevertheless income in the hands of the annuitants, the trustees being assessable under Gen. R. 21 (*Peirse-Duncombe's Trustees v. C.I.R.* (1940), T.R. 247).



### § 11.—War taxation and Annuities.

The heavy increase in the rates of income tax and sur-tax produced a situation which was not contemplated by the parties who, before the war, provided for payment of annuities, alimony, interest, etc., at constant net amounts, and the law was amended so that the payments should be the same as if the rates of tax had not been increased, thus passing the burden of the increased tax on to the payee of the income (§§ 25, 27—1941).

The provisions apply for 1941-42 onwards to any arrangement made in writing before 3rd September, 1939 (the outbreak of the war), and not varied on or after that date but before the passing of the 1941 Act (22nd July, 1941) (*Fitzgerald v. C.I.R.* (1944), T.R. 163), for the payment, whether periodically or otherwise, of a stated amount free of income tax or free of income tax other than sur-tax, provided the provision for the payment is contained in—

- (a) any deed or other instrument;
- (b) any will or codicil (a will is “made” at the date of death (*Berkeley v. Berkeley* (1946), 201 L.T. 310, overruling *re Waring* (1942), T.R. 155));
- (c) any order of the Court;
- (d) any local or personal Act of Parliament; or
- (e) any contract.

For this purpose, the term “free of tax payment” is used in a specially defined sense, as including not only provisions in wills or Court orders, but also provisions for the payment of such sum as will after deduction of income tax be equal to a stated amount. The term “a stated amount” includes a stated

fraction of the gross amount of any specified income (*i.e.*, before income tax has been charged thereon), but does not include a stated fraction of the net amount of any specified income.

The following have been held to be “a stated amount” :—

- (a) A payment under a Will in any year to make up the amount by which the income falls below £500 after deduction of tax at the current rate (*In re Bird* (1944), T.R. 1).
- (b) The £1,200 in a case where, after a decree of divorce, the husband entered into an agreement with the wife assigning his life interest in the trust fund of their marriage settlement and undertaking to pay to her every year such sum “as will, when added to the net income arising from the trust fund in that year, leave a sum of £1,200 after deduction of Income Tax at the current rate” (*Holmpatrick v. Ainsworth* (1943), T.R. 317).
- (c) Such an amount as in any year was required to make the annual net income of any estate up to £5,000 a year clear of all death duties and income tax (*In re Earl of Berkeley* (1945), T.R. 23).

The provisions do not affect—

- (a) any provision in any document which falls within Gen. Rule 23, so that an agreement for the payment of interest “free of tax” (using the term in its ordinary meaning and not that stated above) will still be invalid in that respect, and the payer can deduct tax as usual ;

- (b) any provision for a free of tax payment by virtue of any provision in the same or any other deed, instrument, will, codicil, order, local or personal Act, or contract, which contemplates rises in the rates of tax, whereby the payments thereunder have ceased, or in the event of further rises in the rates of tax, may cease to be wholly free of tax (whether including or excluding sur-tax); this excludes any case where the obligation to pay free of tax carries an over-riding limit, *e.g.*, where trustees are required to pay the income tax liability up to a rate of, say, 6/- in the £;
- (c) any dividends or shares of profits. In this case, the rights of too many other people are affected for Parliament to intervene, *e.g.*, the free of tax provision for a preference dividend has affected the price of transfers not only of the preference shares but of all other classes of shares long prior to the consideration of the legislation, and will continue to do so.

In the case of emoluments assessable under Sch. E, special provisions are applied (*see* Chap. XI, § 9).

The modifications enacted are as follows:—

(1) The stated amount of any payment falling to be made in any year of assessment for which the standard rate is 10/- in the £, has effect as if the stated amount were reduced to twenty twenty-ninths thereof. This is to preserve the gross equivalent at the amount applicable when the rate of tax was  $\frac{5}{6}$  in the £ (£1 less  $\frac{5}{6} = \frac{14}{6}$ ; £1 less 10/- = 10/-; hence the ratio 10 :  $14\frac{2}{3}$  or 20 : 29). When the rate of tax is 9/-, the fraction is twenty-two twenty-ninths, and so on,

increasing the numerator by one for each sixpence by which the rate of tax is reduced (§ 20—(No. 2) 1945).

### Illustration (1).

A mortgagor had agreed to pay interest on a mortgage for £1,450 at such rate as after deduction of income tax at the current rate from time to time would be equal to 3 per cent. The amount payable in 1945-46 will be £43 10s. 0d.  $\times \frac{2}{3} = £30$ , and that payable in 1946-47 will be £43 10s. 0d.  $\times \frac{2}{3} = £33$ , each being equivalent to £60 gross. The payer therefore suffers the same amount as if tax were at 5/6, and the payee bears the extra tax thus :—

		1945-46.	1946-47.
Gross amount of £43 10s. 0d. with tax			
at 5/6 .. .. .	£60 0 0	£60 0 0	
Tax at 5/6 .. .. .	16 10 0	16 10 0	
	<hr/>	<hr/>	
“ Old ” payment .. ..	43 10 0	43 10 0	
Tax at S.R. - 5/6 = 4/6 .. ..	13 10 0	3/6 10 10 0	
	<hr/>	<hr/>	
“ New ” payment .. ..	<u>£30 0 0</u>	<u>£33 0 0</u>	

The annual payment is therefore £60 gross, and not £87 (1945-46) or £79 2s. 0d. (1946-47) as it would have been had the new legislation not been passed. It must not, of course, be overlooked that the provisions only affect the amount payable; once it is calculated, the gross amount is an annual charge of the payer and income, taxed at source at the standard rate in the £, of the payee. If the recipient is exempt from tax, his repayment will enable him to enjoy the same cash income as if the pre-war rates of tax had continued; if liable to tax, he bears the war increase.

(2) If the provision is for a payment free of income tax (and not merely free of income tax other than sur-tax) *e.g.*, an annuity by will free of income tax, the payer has to pay to the payee of the stated sum an amount sufficient to discharge the latter's sur-tax thereon. In such a case, the sum necessary to make good the sur-tax for the year preceding the year of assessment is reduced to twenty twenty-ninths (1946-47 twenty-two twenty-ninths) of the sum which

would have been sufficient for the purpose if the sur-tax rates in force for 1937-38 had applied to the year for which the sur-tax is payable.

(3) A person entitled to a free of tax payment is entitled to the following adjustment of his sur-tax for 1940-41: his total income for 1940-41, so far as it is ascribable to his rights to such payment, is reduced to what it would have been if in his case—

- (a) the 1937-38 sur-tax rates had applied also to 1938-39, 1939-40 and 1940-41; and
- (b) the 1938-39 standard rate ( $\frac{5}{6}$ ) and allowances had applied also to the years 1939-40 and 1940-41; and
- (c) the rights and liabilities of the persons concerned had been modified accordingly.

The purpose of this provision is to compute the income from the source in question as if the 1937-38 rates of sur-tax and 1938-39 standard rate and allowances had continued. At first sight it might appear unnecessary to refer to so many years, but consideration will show that sur-tax for 1938-39 is payable in 1939-40, and the tax paid in 1939-40 will affect payments of free of tax annuities under a will in 1940-41 (cf. *Le Fevre v. Pettit*, *supra*).

(4) Where, as in *Le Fevre v. Pettit* (*supra*), the payee has to account to the trustees for so much of any relief from income tax which he receives as is ascribable to the payment he receives—

- (a) the payee's liability to account is limited to twenty-two twenty-ninths (prior to 1946-47, twenty twenty-ninths) of what he would have been accountable for if the 1938-39 standard rate and allowances applied to the year of

assessment and the provisions in (1), (2) and (3) above had not been passed ; and

(b) the relief to be given is to be calculated as if—

(i) the gross equivalent of the payment were what it would have been at 1938-39 standard rate and allowances, and (1)-(3) above did not apply ; and

(ii) that gross sum had borne tax at the standard rate in the £.

The payee is only receiving twenty-two twenty-ninths (or twenty twenty-ninths prior to 1946-47) of the original annuity, and it is therefore proper that he should account to the trustees for a similar proportion of what the repayment would have been if calculated by reference to the standard rate and allowances of 1938-39. The trustees are put in the position that the same gross income will satisfy the net cost (annuity less refund by annuitant) as if the 1938-39 rates still obtained. The annuitant therefore bears the increased tax, unless he is exempt, when he enjoys the same income as pre-war.

In *C.I.R. v. Cook* ((1945), T.R. 259), Viscount Maugham made it clear that in these free-of-tax bequests by will, a benevolent construction had to be applied if the plain intention of the will was to be carried out. That intention could be achieved by the simple means of holding that the testator must have intended to give, in addition to the fixed annuity, such a sum as would enable the trustees in each year to discharge the Income Tax on the total amount of the fixed annuity and that additional sum, and to pay the balance, which in the normal case would be the exact

amount of the stated annuity, to the annuitant. In other words, the amount of tax is an additional gift, and is included in the income of the annuitant; the income from the annuity is the net annuity plus such sum that, when the tax is levied upon the total amount, the net annuity is left.

The gross amount of the annuity should be found by grossing the net sum at the standard rate in the usual way, *i.e.*, with tax at 9/- in the £, the gross amount of £110 free of tax is £200. The Revenue practice has been modified to give effect to this decision. (It was also argued by the Revenue that the annuitant ought to be repaid only the amount she was entitled to retain, not the amount she had to hand to the trustees, but this argument failed.)

#### Illustration (2).

Annuity under the Will of a testator who died in 1938, £174 free of tax. Annuitant single and over 65 years of age.

1947-48

Annuity payable  $\frac{22}{80} \times £174 = \underline{£132}$ .

		Tax		
		£	s.	d.
Gross equivalent ..	£240	108	0	0
Allowances—				
Age .. ..	£40			
Personal ..	110			
	<u>150</u>			
	<u>£90</u>			
£50 at 3/- ..	£7 10 0			
£40 at 6/- ..	12 0 0			
	<u>19 10 0</u>			
Repayable ..		<u>£88</u>	<u>10</u>	<u>0</u>

At 1938-39 rates—

		£	s.	d.
Gross equivalent	£240	66	0	0
Allowances—				
Age .. ..	£48			
Personal .. ..	100			
	—			
	148			
	92			

£92 at 1/8 ..	7	13	4
	£58	6	8

Account to trustees—

for  $\frac{2}{3} \times £58$  6s. 8d. =

Retain .. ..	£44	5	0
	44	5	0
	£88	10	0

Cost to estate—

	1938-39	1947-48
Annuity paid ..	£174 0 0	£132 0 0
Refund .. ..	58 6 8	44 5 0
	—	—
Net cost ..	£115 13 4	£87 15 0

Gross equivalent (5/6) £159 10 11 (9/-) £159 10 11

The annuitant bears the increased taxation, £240 at 3/6 (*i.e.*, 9/- — 5/6) = £42 on the same gross cost to the estate as in 1938-39.

**Illustration (3).**

Had the death taken place in, say, 1940, the position for 1947-48 would have been—

	£	s.	d.
Gross annuity £174 $\times \frac{2}{11}$ =	316	7	3
Allowances—			
Age .. ..	£53		
Personal .. ..	110		
	—		
	163	0	0
	153	7	3
£50 at 3/- .. ..	£7	10	0
£75 at 6/- .. ..	22	10	0
£28 7s. 3d. at 9/- .. ..	12	15	3
	£42	15	3
Deducted at source .. ..	142	7	3
Repayment .. ..	£99	12	0
All to be accounted for to the Trustees.			



**Illustration (4).**

Annuity, free of tax, under Will of testator who died in 1946, £220 ; Annuitant's other income £200, half taxed at source.

Annuitant married.

1947-48					Tax					
					£	s.	d.	£	s.	d.
Gross annuity	..	..	..		400	0	0	180	0	0
Other Income	..	..	..		200	0	0	45	0	0
					<hr/>			<hr/>		
Personal allowance		..	..		600	0	0	225	0	0
					<hr/>			<hr/>		
					180			0 0		
					<hr/>			<hr/>		
					420			0 0		
					<hr/>			<hr/>		
£50 at 3/-	..	..	..	..	£7	10	0			
£75 at 6/-	..	..	..	..	22	10	0			
£295 at 9/-	..	..	..	..	132	15	0			
					<hr/>			162 15 0		
					<hr/>			<hr/>		
Repayable	..	..	..	..				£62 5 0		
								<hr/>		
Account to Trustees for $\frac{1}{2}\frac{1}{2}\frac{1}{2}$					× £62 5s. 0d. =			£41 10 0		
								<hr/>		

It has been held that a settlement transferring shares to trustees on trust to pay certain annuities is not an agreement to which Gen. R. 23 (2) applies. Accordingly a direction that the annuitants shall enjoy their annuities free of tax is valid and § 25, 1941 applies (*Re Goodson's Settlement*, *Goodson v. Goodson* (1943), W.N. 26).

**§ 12.—Executors and Trustees.**

The tax chargeable on a deceased person's income to the date of death is assessable on the executors or administrators, and is a debt due and payable out of the estate (§§ 31 (2), 32 (3), and 34 (4)—1926 ; § 45 (6)—1927 ; § 15 (4)—1930). Assessments upon the executors, etc., for tax due in respect of income prior to the deceased's death, can only be made within the three years following the end of the year

of assessment in which the death occurs (Gen. R. 18), but may be for any of the six years preceding the year in which the assessment is made (§ 29—1923). The deceased is entitled to personal, etc., allowances for the full year in which he died; and his widow (if any) is entitled to a full year's allowances as a single person for the same year. (*See illustration, Chap. XI, § 14.*)

The executors are also liable to pay the tax on any income received after death. Any tax so paid is deducted when paying over the amounts received to the beneficiaries.

The Apportionment Act, 1870, does not affect relations between the taxpayer and the Revenue. Where, therefore, a dividend or interest received after death accrued wholly or in part before death, with the result that, under the Apportionment Act, the proportion to the date of death is credited to capital, that proportion is not income of the deceased, since it was not received during his lifetime, nor is it income available for a beneficiary since it is capitalised (*C.I.R. v. Henderson's Trustees* (1931), 16 T.C. 282). Tax thereon is paid by the executors by deduction or by direct assessment and charged against the capital portion of the dividend or interest.

If, however, the will directs that no apportionment is to be made, so that the dividend or interest accrued to the date of death is actually available for the beneficiaries as income, it appears to be the practice to regard the dividend or interest as all arising since the death.

Similarly an annuity, accruing from day to day but ceasing on the death of the deceased is not his income

for the purposes of a repayment claim; it did not come to him in his lifetime (*Bryan v. Cassin* (1942), T.R. 145).

A trustee is charged with tax, not as trustee, but as the person in receipt of the income of the trust; therefore, untaxed interest received by the trustees or executors, even if mainly or wholly accrued prior to the death of the testator and therefore to be treated *pro tanto* as capital, is assessable in full on the trustees or executors (*Reid's Trustees v. C.I.R.* (1929), 14 T.C. 512) even if the accrued income is that of a deceased non-resident life tenant, so long as the executor is resident here (*Wood v. Owen* (1940), T.R. 463). Otherwise the liability of a beneficiary depends upon residence or domicile. Regard must be had to the circumstances of the beneficiary, not of the trustees, in assessing untaxed income (*Williams v. Singer* (1921), 7 T.C. 387; *Reid's Trustees v. C.I.R.* (*supra*); *Kelly v. Rogers* (1935), 2 K.B. 446).

Sur-tax for the year of death is calculated upon the deceased's income to the date of death, but at the rate for the previous year if that is lower than that for the year of death.

### § 13.—Beneficiaries under a Will or Intestacy.

#### (a) Specific Legatees.

In the case of a specific legacy, the income from the date of death belongs to the legatee. The executor must, when handing over the legacy, pay to the specific legatee the net income received since the death, in so far as it has accrued after death. If the beneficiary is entitled to a repayment of tax thereon, he must claim it in the same manner as any other

tax deducted at source. For the purposes of repayment claims and for Sur-tax purposes, the income is income of the beneficiary for the years in which it arises, although it may be received by him in one sum on the date of the transfer to him of the legacy (*C.I.R. v. Hawley* (1928), 13 T.C. 327). He cannot, however, be assessed to Sur-tax until he receives the income, although it is then related back to the appropriate years.

(b) **Residuary Legatees** (§§ 31, *et seq.*—1938).

The term “executors” is employed in what follows as meaning the personal representatives of the deceased.

It is necessary, in all cases where a person has an absolute interest in residue, to ascertain the income from residue for each year or part of a year of assessment during which the administration of the estate continues. The legatee’s share of that income is deemed to be income in his hands for all tax purposes.

The residuary income is to be found by deducting from the aggregate gross income of the estate for the year of assessment—

- (a) Any annual interest, annuity, or other annual payment which is a charge on residue ;
- (b) Any expenses incurred in the management of the income which are properly chargeable to income, or would be so chargeable but for some provision in the will.

In (a) and (b) it is, of course, not permissible to deduct again any payment already deducted in arriving at the aggregate income.

- (c) Any income of the estate to which a specific legatee or devisee is entitled, either under a vested or contingent interest.

If the legatee is entitled to the whole residue, the whole residuary income is regarded as his, otherwise his proportionate share must be ascertained. For Sur-tax purposes only, he may deduct any legacy duty paid in respect of his share of the income.

The amount due to a residuary legatee cannot be determined exactly until residue is ascertained. During the course of the administration, therefore, the legatee may receive payments on account from the executors. Such payments in so far as they do not exceed the residuary income of the year are regarded as income of the years in which they are paid, at their gross equivalent as if they were "free of tax." When the administration is completed, the amount of the residuary income arising in each year is computed, and treated as if it had been paid to the legatee in the years in which it arose. Where the actual amount so ascertained is less or more than the amount already treated as his income (*i.e.*, the payments on account), the tax is adjusted by additional assessment under Case VI or by repayment as may be necessary, at any time up to the end of the third year following the year of assessment in which administration is completed.

In the above remarks, we have considered only what is termed a "United Kingdom Estate," *i.e.*, an estate the income of which has borne United Kingdom Income Tax by deduction or by direct assessment on the executors. If any part of the income is exempted from tax in the hands of the executors by reason of non-residence or otherwise, the estate is termed a "foreign estate."

In the case of a foreign estate, payments on account are regarded as paid gross, and the legatee's share of residuary income to be gross, assessments being

raised under Case IV of Schedule D as if the income arose from foreign securities. If, however, any of the income of a foreign estate has borne United Kingdom Income Tax, the tax charged on the legatee is to be reduced in the proportion that the income of the trust which has borne United Kingdom tax bears to the aggregate income of the trust, *e.g.*, if one-fourth of the income of the foreign estate has borne United Kingdom tax, the tax charged on the legatee is reduced by one-fourth.

Where the deceased was himself a legatee of an estate, any income of that estate is deemed to be paid to his executors, and must be included in the aggregate income of his estate for the purpose of finding the residuary income thereof.

**(c) Life or shorter Interests (§ 30—1938).**

Any sum paid to a life tenant pending the completion of the administration is deemed to be his income in the year in which it is paid. A payment after the residue is ascertained is deemed to be income of the year in which the residue was ascertained. In the case of a United Kingdom estate the amount paid must be regarded as “free of tax” and be grossed.

As soon as the income of the administration period due to the life tenant is ascertained, it is apportioned over the whole period as if it had accrued from day to day throughout. Any tax under- or over-paid will be adjusted; the adjustment can be made at any time within the three years following the year of assessment in which residue is ascertained. Where tax has to be assessed on the adjustment, the assessment is under Case VI.

In the case of a foreign estate, the sums paid are deemed to be gross receipts, on which the life tenant is assessable under Case IV, but if any part of a "foreign estate" consists of British securities which have already borne tax, an adjustment is made to avoid double taxation. This adjustment takes the form of reducing the tax chargeable by an amount bearing the same proportion thereto as (a) the net amount of the income of the estate that has borne United Kingdom tax (*i.e.*, the income less the tax thereon) bears to (b) the aggregate amount of the income of the estate less the tax borne by the estate.

#### Illustration (1).

The aggregate income of a "foreign estate" comprises £2,000 which has not borne United Kingdom tax and £400 which has borne such tax. With tax at 9s. 0d. in the £, the tax payable by the life tenant must be reduced by—

$$\frac{400 - 180}{2,400 - 180} = \frac{220}{2,220} \text{ of the tax which he would have to pay on the whole income.}$$

For Sur-tax purposes, the corresponding proportion of the life tenant's income from the estate is to be regarded as a net sum after deduction of tax at the standard rate, and be grossed accordingly.

#### Illustration (2).

Assuming that the whole income of the foreign estate as in the previous illustration, was paid to the life tenant, his income therefrom for Sur-tax purposes would be as follows:—

The amount paid to the life tenant is—

Aggregate Income .. .. .	£2,400
Less U.K. Tax on British Income ..	180
	<hr/>
	<u>£2,220</u>

Proportion thereof to be "grossed"  $\frac{220}{2,220}$  of £2,220 = £220

Giving a gross of .. .. .	£400
Balance regarded as gross .. ..	2,000
	<hr/>

Income for Sur-tax purposes .. ..	<u>£2,400</u>
-----------------------------------	---------------

In this illustration, the whole income has been taken into account in order to exemplify the fairness of the provision. In many cases, the life tenant would not be entitled to the whole, but the fraction would apply to whatever income he received.

It may be that a person has an interest in the income for a limited period only. In such case, the above provisions apply to the limited period, substituting references to that period for those to the period of administration.

**(d) Provisions applying to both Absolute and Limited Interests in Residue.**

Where the legatee dies, there must be ascertained according to the relevant rules summarised in (b) and (c) above, the income due to him up to the date of his death, which will then be regarded as part of the aggregate income of his estate.

If different persons have successive interests, the residuary income is divided in accordance with their respective interests.

In a case where income is paid under a discretionary power, only the amounts paid during the administration period are regarded as the beneficiary's income, and not the share of the residuary income as subsequently computed.

**(e) Trust Estates.**

After residue has been ascertained, the above special rules cease to operate.

The trustees of the estate must account for tax on the income, and deduct tax from the payments made to beneficiaries. It was held in *Murray v. C.I.R.* ((1926), 11 T.C. 133) that, where the will provides for charging expenses against income, a beneficiary's income is the grossed share of the actual net income of the estate after the deduction of all



prior charges, including the expenses of management of the trust. This decision was followed in *Macfarlane v. C.I.R.* ((1929), 14 T.C. 532), in which it was said that the question whether administration expenses are or are not to be paid out of income to which the beneficiary is entitled may come in almost every case to be a question depending on the construction of the trust deed.

It appears to be the practice of the Revenue to treat as the claimant's income the actual amount payable to him, grossed at the standard rate, or his proportionate share of the statutory income of the trust, whichever is lower.

Where the will does not provide for charging expenses, it is thought that the share in the statutory income computed according to the Income Tax rules *before* charging expenses should be treated as the beneficiary's income for Income Tax purposes.

If any of the income of the trust is received without deduction of tax, it is common practice to assess the beneficiary to whom it is paid over by the trustee, instead of assessing the trustee who would then deduct tax on paying over the income. This practice enables trustees to give standing orders for interest, etc., on investments to be paid direct to the beneficiary entitled thereto, and also avoids in many instances the payment by trustees of tax which would have then to be reclaimed by the beneficiary.

In *Garland v. Archer-Shee* ((1930), 15 T.C. 693), it was decided that where by the law of the place where a foreign trust is situated (in this case in New York State) the beneficiary is not entitled specifically to the several sources of the trust fund, the mode and time of the application of the income being at the discretion of the trustees, then a beneficiary resident in the United Kingdom is assessable on the amounts received, and not on the full income arising.

An annual sum paid to a trustee as remuneration for his services under a deed of settlement, is an annual payment within the meaning of General Rule 19, and is therefore taxable by deduction (*Baxendale v. Murphy* (1924), 9 T.C. 76).

Where a solicitor is a beneficiary of a trust, and also acts as solicitor to the trust, his professional charges in respect of work done for the trust must be included in his profits for assessment under Case II, notwithstanding the fact that he, as beneficiary, is actually bearing part thereof (*Watson & Everitt v. Blunden* (1933), 12 A.T.C. 496).

Where the Will directed the trustees to take out an educational endowment assurance on the life of the beneficiary, it was held that the income applied in paying the premiums was not income of the beneficiary (*C.I.R. v. Dewar and another* (1931), 16 T.C. 84).

On the death of a person who carried on a business, the assessments are made as if the business had been discontinued on the date of his death and a new business commenced by the executors on that date. No earned income allowance can be given in respect of their share of the trust income to the executors or trustees who carry on the business even where they are beneficiaries, except by concession, where the trustee beneficiary is virtually a proprietor of the business. If, of course, a beneficiary is also an employee of the business, he is entitled to earned income allowance on his remuneration as employee.

The income of a life tenant may include property of which he has the beneficial enjoyment (even pending the ascertainment of residue (*C.I.R. v. Wolverton* (1940), T.R. 123)), in which case the life tenant's

income includes the net annual value of the profits and the gross equivalent of any outgoings paid by the trustees under directions in the will.

A testator's will provided that his residence, furniture, etc., with an annual sum of £2,000 towards the upkeep and expenses, should be available for the use of his widow and his daughter. Both resided in the house, and it was held that one-half of the annual value of the house and of the £2,000 was part of the daughter's total income for Super-tax purposes (*Shanks v. C.I.R.* (1928), 14 T.C. 249). In another case, the will provided that all outgoings in respect of the estate and expenses of keeping up the residence, etc., enjoyed by the life tenant, were to be paid out of the income of the trust estate, and it was held that the amounts actually expended, grossed for Income Tax, were income of the life tenant (*Sutton v. C.I.R.* (1929), 14 T.C. 662).

It will be seen that in the *Shanks* case, no "grossing up" was necessary, as the will limited the payment to £2,000 per annum; whereas in the *Sutton* case, the whole of the outgoings were paid, equivalent to paying the gross amount which, after paying tax thereon, would amount to the sums expended.

In *Miller v. C.I.R.* ((1930), 15 T.C. 25), Lord Warrington of Clyffe said: "the occupier bears and pays the entire tax . . . . because he is the only person in enjoyment of the annual value," and it was held that the annual value of the mansion house and lands occupied rent free by the beneficiary (under terms in the trust disposition) was her income liable to Sur-tax, as well as the sums expended by the trustees in payment of rent, rates, etc., on the house and lands. The fact that she was entitled to have the taxes paid by the trustees did not affect her position as occupier in her own right, and the annual value of her beneficial enjoyment was income for the purposes of the Act (being of a nature to be included in a claim for allowances) and liable to Sur-tax.

Where trustees are directed to pay an annual sum to the beneficiary, making good any deficiencies in such sum out of capital, any amount so paid out of capital is none the less income of the beneficiary (*Williamson v. Ough* (1936), 20 T.C. 194); the amount paid out of capital is subject to General Rule 21, but is not to be "grossed up" even if the annual sum is given free of tax (*John Morant Settlement Trustees v. C.I.R.* (1947), T.R. 309).

### § 14.—Widows.

As has already been stated, a widow is assessed as a single person as from the date of her husband's death. Her income to the date of his death is included with his, but as from that date it is assessable upon her. Where she owns investments in her own right, any untaxed interest therefrom continues to be assessable under Case III, on the preceding year basis, irrespective of the fact that prior to the death her husband was assessed in respect of her income (*Leitch v. Emmott* (1929), 14 T.C. 633). This decision would appear to apply to any income from her separate sources, and the assessments upon her income for the year of death should be split between her late husband and herself on a time basis.

#### Illustration.

A died on 31st August, 1946. His business profits, as adjusted for Income Tax purposes, were:—Years ended 30th September, 1945, £1,200; 1946, £1,800. Dividends were received on 31st May, 1946, of £300 (gross amount), and on 15th August, 1946, of £200 (gross amount).

A's wife was also in business on her own account. Her adjusted profits were:—Years ended 31st December, 1945, £600; 1946, £500. She also held £12,000 2½% Consols.

A's will provided that his widow was to be paid an annuity of £600 per annum, by half-yearly instalments, the first to be paid six months after death.

There were two children under 16.

be assessed as discontinued and recommenced, and the widow can, therefore, insist on this basis if it benefits her.

**§ 15.—Profits from Betting, Illegal Transactions, etc.**

The Acts charge tax on “profits,” drawing no distinction between legal and illegal sources, and there can be a trade within the charge to Income Tax which is either in whole or in part an illegal trade (*Mann v. Nash* (1932), 16 T.C. 523). Even if the trade is illegal, the profits can be assessed, *e.g.*, ready-money and street betting, though illegal businesses, have been held to be assessable (*Southern v. A.B. and v. A.B. Ltd.* (1933), 12 A.T.C. 203).

A person who attends races and systematically bets is exercising the vocation of betting, and is liable to assessment (*Partridge v. Mallandaine* (1886), 2 T.C. 179). But a person whose means of livelihood is betting on horses from his private address with bookmakers at starting prices only, is not in receipt of profits or gains assessable to income tax, Schedule D, either under Case I or Case II, as from a trade or vocation, or under Case VI (*Graham v. Green* (1925), 9 T.C. 309). The distinction appears to be between *professional* and *private* betting.

**§ 16.—Building Societies “1935 Arrangement.”**

A special arrangement has been entered into between the Inland Revenue and the building societies, in order to obviate the large number of small adjustments of liability which would be involved under the ordinary rules, in view of the fact that the majority of such societies’ transactions are with persons either exempt from tax or liable only at the reduced rate.

Briefly, the position under the current arrangement is that—

- (a) Persons investing their capital in shares or deposits of a building society receive the interest without deduction of tax, but are not liable to pay any tax thereon nor can they reclaim tax by reference to such income. For Sur-tax purposes, however, the actual amount received must be included in the statutory total income, and Sur-tax paid thereon.
- (b) Persons paying interest to a building society do not deduct Income Tax. They are, therefore, entitled to set off such interest against their total income in the same way as bank interest. Normally, the interest is deducted from the net annual value of the property, but if relief cannot be given in this way, tax will be repaid, unless the borrower's income is so small that he has no liability to pay tax at all.
- (c) The building society pays tax on its profits without deducting interest paid, but pays at a reduced rate on that part distributed as interest to any shareholder or depositor whose total holding does not exceed £5,000. The reduced or "composite rate" is changed from time to time to approximate to the average effective rate at which shareholders, etc., are paying tax.

The following are the main provisions of this arrangement :—

*Assessment upon Society.*

The society consents to be directly assessed to income tax under Schedule D for each year of assessment for which the arrangement is in force, upon the following amounts :—

AMOUNT.

(a) The amount credited to investors as dividends or interest in the society's year ended in the preceding year of assessment, or if the society has so elected, the amount credited in the accounting year ended in the year of assessment.

(b) The amount of Income Tax paid by the society for the preceding year of assessment, in respect of the society's liability under (a) above or under this heading (b), or, if the "actual" basis has been selected on the excess of the sum of the two following amounts over (a):—

(i) such an amount as after deduction of tax at the standard rate is equal to such part of (a) as is chargeable at the standard rate, and

(ii) such an amount as after deduction of tax at the composite rate is equal to the balance of (a).

(c) The amount by which the whole profit of the society for the same accounting year exceeds the amounts under (a) and (b).

RATE OF TAX.

(1) The standard rate in respect of dividends or interest arising from—

(i) any investment or investments exceeding £5,000, in the aggregate, of any investor (husband and wife being treated as one person for this purpose);

(ii) any investment, of whatever amount, held by, or on account of, or in trust for any incorporated company or incorporated society (not being a company or society entitled to exemption from tax under Schedule D); and

(2) The composite rate in respect of the amount credited as dividend or interest to other investors.

The composite rate.

The standard rate.

The whole profit is to be ascertained by deducting the working expenses from the total receipts for the accounting year, in accordance with the rules of Case I of Schedule D, subject to the following provisions:—

(a) Losses (or any profits) arising on the realisation of properties mortgaged to the society will be included in the computation, but any provision in anticipation of such losses or profits will be excluded.

- (b) Profits or losses arising on the realisation of investments will be excluded.
- (c) All rents received (including those from properties in possession) will be included, and rents paid will be allowed as a deduction.
- (d) No deduction will be allowed in respect of the annual value of property occupied by the society.

The composite rate is varied from time to time. It is now 6s. 0d. in the £ (subject to any change that may be made in a second Finance Act, in 1945). Post war credit is calculated at 7½d. in the £ (the difference between 6s. 0d. and a notional composite rate of 5s. 4½d.).

### *Set-off of Taxed Income.*

Where the receipts of the society for any accounting year include income upon which Income Tax has been paid at the source, the amount chargeable for the following Income Tax year (or if the "actual" basis has been chosen, for the same year) at the standard rate will be reduced by the gross amount of such income. If that gross amount exceeds the amount chargeable at the standard rate, there will be deducted so far as possible from the amount chargeable at the composite rate an amount bearing the same proportion to the excess as the standard rate bears to the composite rate. In any case where, after allowing such set-off, there remains a balance of the said taxed income, the society may claim repayment on the amount of that balance at the standard rate of tax for the year of assessment in which the said accounting year ends (or if the actual basis has been chosen, for the same year).

All property owned by the society, whether let or in its own occupation, and also all property in the hands of the society as mortgagee in possession, is from the date of the society's entering into possession,



to be exempted from Income Tax, Schedule A, except in respect of ground or lease rents, if any.

*Liability of Investors.*

Investors will be required to include dividends or interest in their returns of total income for Income Tax (and Sur-tax) purposes. No charge to Income Tax will be made upon investors in respect of such income from the society, but it will be included in total income for the purpose of charging Sur-tax.

No repayment of tax will be made in respect of income derived from investments with the society, and the society will not issue any certificates of payment of tax in respect of such income.

*Mortgage Interest Paid to the Society.*

A borrowing member who has no taxable income will not have to account for tax on such mortgage interest.

A borrowing member who has taxable income is to be relieved from the tax applicable to such mortgage interest. Relief will be allowed by the Inspector of Taxes upon a certificate, sent to him by the secretary of the society, of the amount of mortgage interest paid. For mortgages taken out before the 1st April, 1935, the certificate will be for the annual period corresponding to that adopted for 1934-35. For mortgages taken out on or after the 1st April, 1935, the certificate will be given for the income tax year.

In the first and last years of a mortgage the certificate will be given as soon as practicable after commencement or termination, as the case may be. In other years the society must certify annually, not later than the 15th June (1) the interest to be paid in the current year (so that provisional relief may be granted

accordingly) and (2) the interest actually paid in the year immediately preceding. Where under (1) an exact forecast of the interest is not possible, an estimate must be made upon a fair and reasonable basis. In those "open account" cases where such estimates are impracticable, local arrangements are made with a view to certificates being given as early as possible.

### *General.*

A certificate by the auditor of the society will be required of the accuracy of the amounts returned for Schedule D assessment. The society agrees to furnish a copy of its statutory annual account and statement to the Inspector of Taxes for the district in which its head office is situated, and also to permit any duly appointed officer of the Commissioners of Inland Revenue to test the accuracy of the amounts returned, or to verify the correctness of any certificate given under the arrangement, by inspection of the books and accounts of the society.

This arrangement operates from year to year until discontinued by notice in writing given by the Board of Inland Revenue or by the society. Such notice must be given at a date between the 6th April and the 6th July, and will take effect as from the 6th April following the date of notice.

The society will facilitate statistical investigation by the Inland Revenue Department of the working of the arrangement by furnishing extracts of the payments of dividends or interest. These extracts will give the name and address of each investor, the amount of his investment, and the amount of dividends or interest thereon, where the investment amounts to £1,000 or more, and similar particulars for a five per cent. sample of investments below £1,000.

The adoption of the arrangement does not prejudice the right of the society to appeal to the General or Special Commissioners if any dispute arises as to the computation of the whole profit (*e.g.*, a dispute as to the admissibility of an item of expenditure as a deduction in the computation).

### *Illustration (1).*

A had an investment income of £2,900, and building society interest received "free of tax" amounted to £93. He owned his dwelling house, assessed under Schedule A at £100 net, on which for the year he paid mortgage interest of £60 to a building society. A was a married man with five children under 16.

## COMPUTATION, 1947-48.

				Income Tax.		
				£	s.	d.
Dividends, etc.	..	..	..	£2,900	1,305	0 0
Building Society interest received	..	..	..	93		
House—Net Annual Value	..	..	..	100		
Less Building Society Mortgage Interest	60			40		
Statutory Income for Sur-Tax	..	..	..	£3,033		
Deduct Building Society interest received						
—not assessable to Income Tax at						
Standard Rate	..	..	..	93		
Income chargeable to Income Tax	..	..	..	2,940		
Deduct Allowances—						
Personal	..	..	..	£180		
Children (5)	..	..	..	300		
Sur-Tax.				480		
£2,000		Nil.				
500 at 2/-	£50	0 0				
500 at 2/6	62	10 0	Taxable Income	..	..	£2,460
33 at 3/6	5	15 6				
£3,033	£118	5 6	Chargeable—	£	s.	d.
			£50 at 3/-	..	..	7 10 0
			£75 at 6/-	..	..	22 10 0
			£2,335 at 9/-	..	..	1,050 15 0
						1,080 15 0
			Tax reclaimed	..	..	£224 5 0
The reclaim is made up of—						
Tax on allowances £480 at 9/-	£216	0 0				
Reduced Rate £50 at 6/-	..	15 0 0				
£75 at 3/-	..	11 5 0				
		242 5 0				
Less Schedule A assessment—						
£40 at 9/-	..	..	..	18	0 0	
As above	..	..	..	£224	5 0	

## Illustration (2).

B, a single man, has an earned income of £250, and received interest on a deposit in a building society of £20.

## COMPUTATION, 1947-48.

Earned Income	..	..	..	£250		
Less Earned Income Allowance	£42					
Personal Allowance	..	110				
		152		£50 at 3/-	=	£7 10 0
				£48 at 6/-	=	14 8 0
Taxable Income	..	..	..	£98		£21 18 0

B cannot reclaim tax in respect of the Building Society interest received, although if this had been a free of tax dividend, he would have reclaimed tax at 3s. on the balance of his Reduced Rate Allowance, £16, up to the amount of the gross equivalent of the interest.

Interest from a building society is included as part of the statutory total income for the purposes of life assurance allowance and old-age allowance, but the maximum amount of tax available for repayment is the tax suffered on income excluding the building society interest. It is understood that such interest can now be regarded as taxed for the purposes of General Rules 19 and 21.

### Illustration (3).

C (who is over 65 and married) has the income indicated in the following repayment claim; 1946-47.

	Gross.	Tax paid.		
	£	£	s.	d.
Business Profits .. .. .	200	—		
Bank Interest .. .. .	20	—		
House, N.A.V. .. .. .	22	9	18	0
Taxed Dividends .. .. .	136	61	4	0
Building Society Interest * .. ..	30	—		
* Note deduction at † below.				
	408	71	2	0
Ground Rent .. .. .	8	3	12	0
	400	67	10	0
<i>Deduct Allowances—</i>				
Age Allowance— $\frac{1}{8}$ th of £400	£50			
Personal .. .. .	180			
	230			
	£170			
<i>Chargeable—</i>				
	£	s.	d.	
£50 at 3/- .. .. .	7	10	0	
£75 at 6/- .. .. .	22	10	0	
£45 - £30† = £15 at 9/-	6	15	0	
		36	15	0
Repayable .. .. .		£30	15	0

\* Building Society Interest received is not chargeable to tax.

## Illustration (4).

The following repayment claim for the year 1947-48, is made by D, who is over 65.

			Tax paid.	
			£	s. d.
Director's fees .. ..	45	0 0	—	—
Taxed Dividends .. ..	400	0 0	180	0 0
Building Society Interest ..	60	0 0	—	—
			<hr/>	
			505	0 0
<i>Deduct</i> Margin .. ..	5	0 0	<hr/>	
			500	0 0
<i>Deduct</i> Allowances—				
Age $\frac{1}{4}$ th of £500	£83	6 8		
Personal ..	110	0 0		
			<hr/>	
			193	6 8
			<hr/>	
			£306	13 4
			<hr/>	
Chargeable—	£	s. d.		
£50 at 3/- .. ..	7	10 0		
75 at 6/- .. ..	22	10 0		
121 13s. 4d. at 9/- (ex- cluding B.S. Interest) ..	54	15 0		
			<hr/>	
			84	15 0
<i>Add</i> $\frac{3}{4}$ Margin over £500 ..	3	15 0	<hr/>	
			81	0 0
			<hr/>	
Repayable .. ..	£99	0 0	<hr/>	

## § 17.—Penalties.

Various penalties are enforceable under the Income Tax Acts for non-fulfilment, by persons assessable, of their statutory duties, of which the following are the most important :—

Under § 107, the penalty on any person—required by the Act to deliver any list, declaration, or statement—refusing or neglecting so to do or negligently making a return incorrectly, within the time limited by the notice, is, if proceeded against before the General Commissioners, a sum not exceeding £20, and treble the tax chargeable (added to the assessment), or, if proceeded against by action or information in any Court, a *sum* of £20 and

treble the tax which ought to be charged (§ 23 (2)—1923). The same penalty applies where an incorrect return is made on a form provided by the Inspector of Taxes. The time limit is deemed to expire on the date the return is delivered to the Inspector (§ 28—(No. 2) 1945).

Under § 100, every person upon whom notice is served requiring him to make a return of any profits, accounts or income chargeable under Schedules D and E is liable on default to a penalty under § 107, whether he is or is not chargeable with tax; but the penalty in the case of a person who is not found to be chargeable with tax shall not exceed £5 for any one offence.

Under § 146, where a person has refused or neglected to deliver any statement or schedule, and it is found that an increased assessment ought to be made, a penalty can be inflicted not exceeding treble the amount of the tax payable; but where the statement or schedule is incomplete, the penalty must not exceed three times the amount of the tax on the amount of the additional assessment.

Under § 127, where a person has been given notice of a surcharge by the Inspector (where the latter discovers that the original assessment was inadequate) and submits a new return or written notice that he abides by his original return, and in any such declaration wilfully and fraudulently declares anything which is false, he is guilty of a misdemeanour, and liable to imprisonment not exceeding six months, and to a fine not exceeding treble the tax surcharged, as the Court may order.

Under § 139, where a person has been required by the Commissioners to deliver any schedule and such person fails to do so, he shall be liable to a penalty not exceeding £20, and treble the tax at which he ought to be assessed. A similar penalty is enacted by Rule 14, Schedule A, No. IV, in respect of returns under Schedule A, for wilfully failing to deliver or produce relevant documents.

Under § 144, a person who after being duly summoned to appear before the General Commissioners (a) neglects or refuses to appear at the time and place appointed, or (b) appears, but refuses to be sworn or to subscribe the oath, or (c) refuses to answer lawful questions touching the matters under consideration, shall forfeit a sum not exceeding £20. The penalty in respect of (b) and (c) does not apply to any clerk, agent or employee of the person assessed.

Under § 30, the penalty for making fraudulent claims for any allowance or deduction, or fraudulently concealing or untruly declaring any income or any sum which he has charged against or deducted from, or is entitled to charge against or to deduct from another person, or fraudulently making a second claim for the same cause, is £20, and treble the tax chargeable in respect of all

the sources of his income. This means treble the tax chargeable on the whole income for the year of assessment, whether made by deduction or not, and not treble the tax on the income still chargeable as not having already borne tax. For aiding and abetting the penalty is £500 (§ 23—1923). The penalty can be enacted wherever there is a false return, even if the concealment of income does not affect the amount of the allowances (*Attorney-General v. Lloyds Bank (Lillicrap's Exors.)* (1944), T.R. 165).

Section 40 (4), provides for a penalty of £100 for fraudulent claims for exemption under §§ 37-39 (charities, friendly societies, etc., see p. 345) in respect of interest, etc., chargeable under Schedule C, and if a person makes such a claim on his own behalf, he is, in addition, liable to be charged treble the tax so chargeable.

Under § 132, the penalty on persons fraudulently changing their residence, or converting property, or delivering false statements, or guilty of other fraud, is treble the amount of the excess tax chargeable; and for aiding and abetting, the penalty is £500 (§ 23—1923).

Under Rule 10, Schedule A, No. V, where a person makes any false or fraudulent claim under Rule 9 for abatement of an assessment in respect of loss by flood or tempest, he shall forfeit £50 and treble the tax charged on him in respect of the lands. Under Rule 11, the penalty for aiding or abetting is £100. Rule 3, Schedule B, extends these rules to Schedule B.

Under § 34, any person guilty of any fraud or contrivance in making application for relief, in respect of loss under the operation of that section, is liable to a penalty of £50.

Under § 44 (3)—1927, if any person liable to Sur-tax fails without reasonable excuse to make a return, or to give to the Special Commissioners before 30th September next following the end of the year of assessment, notice that he is chargeable to Sur-tax, he shall be liable to a penalty not exceeding £50, and after judgment has been given for that penalty, to a further penalty of the like amount for every day during which the failure continues. Similar penalties are imposed in relation to particulars to be furnished of dealings in assets *cum dividend*, so that Sur-tax is avoided (§ 33—1927).

Under § 225, the fine for obstruction of officers in the execution of their duties is £100.

Under § 227, a person found guilty of knowingly making a false statement or representation is liable on summary conviction to six months imprisonment with hard labour. If, however, the proceedings are taken under the provisions of the Perjury Act, 1911, the penalties are much more severe.

A penalty of £100 is imposed for failure to furnish particulars of tax deducted under General Rule 21 (§ 26—1927), and a penalty

of £50 is imposed by General Rule 23, upon any person who refuses to allow a deduction of tax authorised by the Acts.

Under § 23, 1923, proceedings for the recovery of any fine or penalty incurred under the Income Tax Acts may be commenced within six years next after the fine or penalty is incurred. But where any fraud or wilful default is involved, in connection with Income Tax for 1936-37 or any subsequent year, there is no time limit for making additional assessments, and the time for proceedings for the recovery of any fine or penalty is extended to three years after the final determination of the tax covered by the assessments (§ 33—1942). This does not extend the time for assessments on or proceedings against personal representatives of a defaulter.

The Commissioners of Inland Revenue or the Treasury may, in their discretion, mitigate any fine or penalty (§ 222) except under § 132 and Sch. A, No. V, Rule 10, and Sch. B, Rule 3. Penalties may be added to and collected with the assessment (§ 223). But the High Court has no power to mitigate penalties under §§ 30, 32, 34, 40, 102 (2), 107, 132, 225, § 33 (6)—1927, or § 44, 1927, or under Schedule A, No. IX, Rule 5; Schedule C; Schedule A, No. V, Rule 11; Schedule B, Rule 3; or General Rule 23.

Under § 162, the collector is empowered to distrain for non-payment of tax, upon the premises, etc., in respect of which the tax is charged, or the person charged by his goods or chattels.

Under § 169, any tax charged under the Act may be sued for and recovered by proceedings in Court.

Penalties are rarely exacted to the full extent provided by the Act, except in very grave cases. The Commissioners usually exercise their powers to mitigate the penalties, provided that, where they discover the default, a sum in respect of compound interest and part penalties is paid. Where the taxpayer makes the disclosure the sum exacted is smaller. (See also section on "Back Duty.")

A penalty under § 221 (2)—1918 (which provides for suing for fines, etc.) can be recovered from the personal representative of the deceased (*Attorney-General v. Canter* (1939), 1 A.E.R. 13).

How far this case extends is not certain, however, as the Master of the Rolls suggested that penalties imposed under §§ 132, 146, and similar sections could



not be made against executors, owing to the absence of machinery for bringing them before the Commissioners.

### § 18.—Back Duty.

The term “back duty” is the accepted name given to tax which has not been charged in past years. High rates of tax have tempted many taxpayers to evade their legal burden, with consequent serious loss to the Revenue. Other taxpayers have evaded their liability through ignorance or carelessness.

Although such evasion has been practised, consciously or unconsciously, by a very small minority, the tax so lost to the Revenue is undoubtedly a substantial sum, throwing a correspondingly heavier burden upon the honest and careful citizen.

Evasion must not be confused with legal avoidance. “No man in this country is under the smallest obligation, moral or other, so to arrange his legal relations to his business or to his property as to enable the Inland Revenue to put the largest possible shovel into his stores. The Inland Revenue is not slow—and quite rightly—to take every advantage which is open to it under the taxing statutes for the purpose of depleting the taxpayer’s pocket. And the taxpayer is in like manner entitled to be astute to prevent, so far as he honestly can, the depletion of his means by the Revenue” (*The Lord President (Lord Clyde) in Ayrshire Pullman Motor Services and David M. Ritchie v. C.I.R.* (1929), 8 A.T.C. 531, at p. 537). This dictum still holds good, though it is regarded as unpatriotic to-day to enter into devious channels to avoid tax. Moreover, most of the loopholes have been closed.

The penalties for evasion have already been outlined, and in cases where a practitioner is called in to deal with a "back duty" case, he should make himself thoroughly familiar with the exact words of the sections of the Act to see which penalties are relevant. Where fraud is absent, only §§ 107 and 222 are relevant—see also § 23, 1923, however.

It is under § 222 that the Commissioners of Inland Revenue derive their powers of "bargaining," whereby an agreed lump sum payment is accepted in settlement of back duty, interest and penalties.

Students are often at a loss to understand how the Inland Revenue Authorities can open "out of date" years, when § 29, 1923, enacts that assessments may be amended, additional assessments made, etc., only within six years after the end of the year to which the assessment relates, or the year for which the person liable to Income Tax ought to have been charged, and § 33, 1942, only extends this time in the case of fraud or wilful default. The penalty provisions provide an answer—the taxpayer usually prefers to pay the back duty and interest, with a sum by way of mitigated penalties rather than be mulcted in the possible penalty under § 107, 1918, or § 23 (2)—1923, of £20 plus treble the amount of tax which ought to have been paid for each of the six years *within* the time limit, and possible publicity if he is prosecuted. Moreover, the penalties imposed by § 107 (1) and (3) are incurred not merely by non-delivery of a return, but by delivering a return which is not true and correct (*Attorney-General v. Till* (1909), 5 T.C. 440).

Where a person who in making a claim for or obtaining any allowance or deduction or in obtaining a certificate for repayment in respect of relief, is guilty of any fraud or contrivance or fraudulently conceals

or untruly declares any income or annual charges, or fraudulently makes a second claim for the same cause, then § 30 applies. The words "treble the duty chargeable in respect of all sources of income" mean treble the duty chargeable on the *whole income* for the year of assessment in question, and not merely treble the duty on the income still chargeable as not having borne the tax (*Lord Advocate v. McLaren* (1905), 5 T.C. 110; 7 F. 984). "The offence.....is not, in my opinion, an inaccurate, but a false or untruthful declaration..... A charge of untruly declaring seems to me to imply the intention to deceive" (*Per Lord Kinnear*, 7 F. p. 992, *ibid.*).

Section 5, Perjury Act, 1911, should be noted, viz. :—

If any person knowingly and wilfully makes (otherwise than on oath) a statement false in a material particular, and the statement is made—

(a) in a statutory declaration; or

(b) in an abstract, account, balance sheet, book, certificate, declaration, entry, estimate, inventory, notice, report, return, or other document which he is authorised or required to make, attest, or verify, by any public general Act of Parliament for the time being in force; or

(c) in any oral declaration or oral answer which he is required to make by, under, or in pursuance of any public general Act of Parliament for the time being in force,

he shall be guilty of a misdemeanour and shall be liable on conviction thereof to imprisonment, with or without hard labour, for any term not exceeding two years, or to a fine or to both such imprisonment and fine.

The common law may also be invoked.

Section 140 (1) gives relief to a taxpayer who makes full disclosure by delivering statements rectifying his omissions and wrong statements, provided he can be said to have *discovered* his "omission or wrong statement." Where no return has been rendered, the taxpayer is entitled to take advantage of § 140 (2) and deliver a proper statement or schedule before proceedings have commenced. Section 140 (3) authorises proceedings to be stayed where no fraud or evasion was intended.

Fraud must not be confused with negligence. Fraud can only be proved "when it is shown that a false representation has been made knowingly, or without belief in its truth, or recklessly, careless whether it be true or false" (*Lord Herschell in Derry v. Peek* (1889), 14 A.C. 337).

In cases where the taxpayer himself does not initiate the enquiries by disclosure, enquiries leading to the discovery of unassessed income arise in many ways. The Inspector may act on the information given to him by a common informer, or may learn that the taxpayer's mode of life is incompatible with the income returned. Again, the taxpayer's return may disclose new sources of income which lead the Inspector to believe that the taxpayer must have made investments out of sources other than savings. The honest taxpayer in such a case can prove that he has received loans or legacies, won prizes in competitions or sweepstakes, gained money on betting or Stock Exchange dealings, etc., and that his returns were correct; but if in fact his new capital is the result of saving undisclosed income, the Inspector's suspicions are proved to be soundly founded.

Enquiries as to the reason for unusual fluctuations in gross profit may bring to light that the taxpayer has been introducing fraudulent invoices for purchases, suppressing sales, or manipulating stock values. The above instances are by no means exhaustive, but will suffice to indicate to the student that the Inspector's seemingly irrelevant lists of queries on a client's accounts are not always so unnecessary as they appear to be.

Once enquiries have been made, the taxpayer must make the fullest disclosure, in his own interests. Where he is engaged in trade, certified accounts for the years involved should be prepared, if at all possible.

Unfortunately, however, the preparation of such accounts is all too frequently found to be impossible, and the compilation of capital statements (officially termed a "means test") is then the best that can be prepared. It is not within the scope of this work to explain in detail how such statements should be drawn up, since that is a matter akin to the preparation of profit statements where books are kept by single entry, or where no books are kept at all, matters adequately dealt with in book-keeping text books.

The preparation of such statements is usually a matter of the utmost difficulty, owing to the absence of reliable information and records. Bank pass books are frequently the only available records, and these are not usually adequate, since neither do they show details of the items entered therein nor do they contain any evidence of receipts or payments not passed through the bank.

The following outline of a capital statement indicates some of the matters to be investigated in order to arrive at the required figures :—

## A's worth at 6th April, 1936 :—

Dwelling House at cost .. ..	£1,500
Furniture therein .. ..	600
Week-end cottage, at cost .. ..	400
Furniture therein .. ..	100
Business Assets (net) .. ..	5,000
Investments, at cost .. ..	10,000
National Savings Certificates, self and wife, at cost .. ..	775
Loans .. ..	2,000
	<hr/>
	20,375
<i>Less</i> Creditors .. ..	£375
Mortgage .. ..	400
	<hr/>
	775

Net Assets .. .. £19,600

## At 5th April, 1946 :—

Dwelling House, at cost .. ..	£1,500
Furniture therein—	
As at 6th April, 1936 .. ..	£600
Additions at cost .. ..	200
	<hr/>
	800
Business Assets (net) .. ..	14,000
Investments, at cost .. ..	21,000
National Savings Certificates at cost .. ..	800
Loans .. ..	6,000
Deposit Account and Cash .. ..	3,100
	<hr/>
	47,200
<i>Less</i> Creditors .. ..	£200
Loans .. ..	1,000
	<hr/>
	1,200

Net Assets .. .. £46,000

Increase in Assets .. .. £26,400

<i>Add</i> Personal Living Expenses for the period .. ..	7,000
Insurance Premiums (Life), Income Tax and Loan Interest paid .. ..	1,200
Losses on Stock Exchange and betting transactions .. ..	700
Loans made during period, now irrecoverable (not included above) .. ..	1,000
	<hr/>

Carried forward .. £36,300

	Brought forward ..	£36,300
<i>Deduct</i>	Legacies received ..	£8,000
	Bonus Shares sold—proceeds	700
	Matured Endowment	
	Policy .. ..	1,000
	Investment Income, Loan	
	Interest, etc., <i>net</i> ..	5,800
	Deposit Interest .. ..	300
	Profit on Sale of Cottage	
	and Furniture .. ..	50
	Profit on War Savings	
	Certificates .. ..	225
		<hr/> 14,075
	Amount to be taken as business profits	
	and unexplained income for period	<u>£22,225</u>

It now remains to apportion this income over the years covered by the statement, not necessarily equally, as the facts of the case may indicate that in certain years the capital increment may be more or less than in others. Interim capital statements may be desirable. Statements of total income must then be prepared for each year, and the tax computed.

A certificate of complete disclosure is then usually required to be signed by the taxpayer, and the matter of the amount of duty to be paid is then open to argument. A reasonable offer, consisting of the tax under-paid, compound interest and, in appropriate cases, a sum for commuted penalties, should be made, having regard to all the facts and the present financial position of the taxpayer.

When the offer has been accepted by the Inland Revenue, frequently allowing for payment by instalments, the taxpayer is required to sign a written undertaking that he will pay as agreed in consideration of the Revenue Authorities waiving their rights to take proceedings for penalties, and that failure to

pay an instalment will make the whole balance immediately payable. It was held in *Attorney-General v. Johnstone* ((1926), 10 T.C. 758), that the Commissioners of Inland Revenue were empowered by § 222 to accept a sum in composition of penalties in this way, and that such a contract was perfectly legal and binding. Where a person dies after having entered into an agreement with the Commissioners of Inland Revenue to pay an agreed sum in consideration of the compromise of penalties, the deceased's executors are liable to pay the sum agreed (*Attorney-General v. Midland Bank Executor and Trustee Company* (1934), 31 A.T.C. 602).

An important departure from the ordinary rules of law is that if the delinquent fails to make full disclosure and restitution and proceedings are started against the person in question—

- (a) for any form of fraud or wilful default in connection with or in relation to income tax ;  
or
- (b) for the recovery of any sum due from him, whether by way of tax or penalty, in connection with or in relation to income tax,

statements made or documents produced by or on behalf of that person are not inadmissible in evidence against him by reason only that it has been drawn to his attention that—

- (a) in relation to income tax the Commissioners of Inland Revenue may accept pecuniary settlements instead of instituting proceedings ;
- (b) though no undertaking can be given as to whether or not those Commissioners will accept such a settlement in the case of any



particular person, it is the practice of the Commissioners to be influenced by the fact that a person has made a full confession of any fraud or default to which he has been a party, and has given full facilities for investigation, and that he was or may have been induced thereby to make the statements or produce the documents (§ 34—1942).

## CHAPTER XII.

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### THE PROFITS TAX (formerly THE NATIONAL DEFENCE CONTRIBUTION).

NOTE.—The abbreviations “N.D.C.” and “P.T.” respectively are used throughout this Chapter to mean National Defence Contribution to 31st December, 1946, and Profits Tax thereafter.

#### § 1.—Principles.

This tax, which is in addition to Income Tax, was imposed by the Finance Act, 1937, as from 1st April, 1937, continued by the Finance Act, 1942, renamed by the Finance Act, 1946, and materially amended to Finance Act, 1947. N.D.C. was charged on—

- (a) All trades or businesses carried on in the United Kingdom, and
- (b) All trades or businesses carried on elsewhere by persons ordinarily resident in the United Kingdom.

As from 1st January, 1947, the tax does not apply to any business unless it is carried on by a body corporate, or by an incorporated society or other body; *i.e.*, individuals and partnership of individuals are exempted.

If a company is a partner, it will be regarded as carrying on the business, but the profits or losses of the business will be confined to its share of the partnership profits or losses. If the company is also carrying on another business, the profits from the partnership are to be computed without abatement, added to its other profits, and the total, if appropriate, abated.

N.D.C. was charged at—

5 per cent. in the case of companies and other corporate bodies.

4 per cent. in the case of individuals carrying on business as sole traders or in partnership.

Profits Tax is charged at 25 per cent., with relief for profits not distributed to proprietors (termed “non-distribution relief”) of 15 per cent. The effect is, therefore, to charge 10 per cent. on profits ploughed back into the business, and 25 per cent. on profits distributed. As will be seen later, the calculation of the distributions is according to formulæ laid down in the Acts.

For N.D.C., the charge was on the profits of the trade or business, although the type of proprietorship determined the rate of charge. If a person carried on more than one trade, each was a separate source chargeable as if there were no other source.

For Profits Tax, however, all trades or businesses carried on by the same person are treated as one business (if liable to Profits Tax ; a business not within the charge would be omitted from the aggregation) (§ 43—1947).

The assessment is based on the actual income of the accounting period, adjusted according to the rules of Schedule D, Case I, with certain modifications, that will appear hereafter.

The profits are ascertained by adjusting the accounts of each accounting period which falls wholly or partly after 31st March, 1937, but only such portion of any accounting period which falls after that date is a “chargeable accounting period” for which N.D.C. or P.T. is payable.

The N.D.C. or P.T. payable in respect of any chargeable accounting period is to be debited in the accounts in arriving at the adjusted profits for Income Tax purposes (§ 25—1937), *i.e.*, the N.D.C. or P.T. reduces the profits of the accounting year on which the Income Tax assessment is based. N.D.C. or P.T. is allowed as a management expense for the purposes of a claim under § 33, 1918.

From 1st April, 1939, to 31st December, 1946, the N.D.C. was an alternative to the Excess Profits Tax, in that where a business was within the scope of both duties, only the higher was payable. In the case of a chargeable accounting period which fell partly before 1st April, 1939, and partly after that date, N.D.C. was chargeable to 31st March, 1939, and the higher of the N.D.C. or E.P.T. thereafter. Similarly, where a chargeable accounting period bridges 31st December, 1946, the higher of E.P.T. or N.D.C. is payable to 31st December, 1946, and P.T. thereafter. The calculation of the tax payable in such cases is explained and illustrated on p. 628.

## § 2.—Trades and Businesses Liable (§ 19—1937).

As already stated, N.D.C./P.T. is chargeable on the profits of all trades or businesses of any description carried on in the United Kingdom, or carried on, whether personally or through an agent, by persons ordinarily resident in the United Kingdom. Whether or not a business is carried on in the United Kingdom is a question of fact. The doctrines of control and ordinary residence have already been explained in Chapter V.

In order to charge N.D.C./P.T. on finance, investment and property companies, it is provided that where

the *functions* of a company or society incorporated by or under any enactment consist wholly or mainly in the holding of investments or other property, the holding of the investments or property shall be deemed to be a business carried on by the company or society (*ibid.*). Industrial and provident societies, co-operative societies, building societies, banks, investment companies, landed estate companies, etc., are thus liable. As will be seen later, where a liable business is not assessable to Income Tax under Schedule D, Case I, its profits must be computed as if its income were liable to be so assessed. Husbandry is a business liable to N.D.C./P.T. (*Wernher v. C.I.R.*); *Leader* (for *Edmund*) *v. C.I.R.*; *British Grolux v. C.I.R.* (1942), T.R. 11).

In the case of stud farms, the business of carrying on the stud farm is severable from the breeding operations carried on for the purposes of the occupier's recreation of racing (*ibid.*).

A profession carried on by an individual or by individuals in partnership was exempted from N.D.C., if the profits of the profession were dependent wholly or mainly on his or their personal qualifications. For this purpose the expression "profession" does not include any business consisting wholly or mainly in the making of contracts on behalf of other persons, or the giving to other persons of advice of a commercial nature in connection with the making of contracts.

In certain types of businesses, *e.g.*, estate agents, some are mainly on one side of the line and some on the other, according to the class of work done. In such a case, the profits are either liable or exempt, according to which side of the line they fall; if two distinct professions are carried on, each must be regarded

separately on its own merits. In the case of estate agents, etc., tenant right valuation and estate management are professional activities (*Escritt and Barrell v. C.I.R.* (1947), T.R. 13).

No such questions arise for P.T., as the charge does not apply to sole traders and partnerships of individuals. The share of a company in the profits of a firm in which it is a partner will be added to its own profits (§ 31—1947).

### § 3.—Trades, etc., exempted from N.D.C. and P.T.

In addition to professions (dealt with above), there are certain other exemptions, *viz.*:—

#### (1) STATUTORY UNDERTAKINGS.

N.D.C./P.T. is not chargeable on the profits of any trade or business carried on by statutory undertakers and consisting wholly or mainly in the rendering in the United Kingdom or a dominion of any of the following services, namely:—

- (a) the supply of water, gas, electricity or hydraulic power ;
- (b) the provision or maintenance of a canal or other inland waterway or a harbour, dock, pier, quay, road, bridge, ferry, or tunnel ;
- (c) the conservancy of a river ;
- (d) the carriage of goods or passengers by railway, or the carriage of passengers by road, or the carriage of goods by canal or inland navigation.

For this purpose, the expression “statutory undertakers” means (i) any local or public authority authorised by or by virtue of any enactment to render any of the above-mentioned services in the United Kingdom or a dominion, and (ii) any other person so authorised who is precluded by or by virtue of any enactment from charging any higher price for those services than that authorised by or by virtue of the enactment or, in the case of a body corporate, is either so precluded or precluded by or by virtue of any enactment from paying a dividend at any higher rate, or distributing by way of dividend any greater amount than that authorised by or by virtue of the enactment. The expression “pier” means a pier wholly or mainly used for loading or unloading goods or embarking or disembarking passengers (§ 19—1937).

In imposing the tax, Parliament considered that these statutory undertakings, being limited as to the charges they may make or profits they can distribute, could not fairly be charged. In the case of undertakings in the dominions, those claiming exemption have to prove that they are restrained in their charges or distributions of profit as stated ; only such undertakings as are owned in the United Kingdom or actually operating under British financial control could be liable in any case.

The expression "dominion" means any British possession, or any territory which is under His Majesty's protection or in respect of which a mandate is being exercised by the Government of any part of His Majesty's dominions (§ 27 (8) (a)—1920).

## (2) NEW UNDERTAKINGS IN THE SPECIAL AREAS.

If the Commissioners appointed for the purposes of the Special Areas (Development and Improvement) Acts, 1934 and 1937, certify that, for the purpose of inducing any persons to establish an industrial undertaking in any of the special areas, it is expedient that those persons, in addition to being provided with financial assistance under Section 3 of the Special Areas (Amendment) Act, 1937, should be given relief in respect of any N.D.C./P.T. which may become chargeable in respect of the profits of the undertaking, the Treasury may agree to remit the whole or any part of N.D.C./P.T. so chargeable (§ 19—1937). This relief can only be given to new undertakings ; those in existence before April, 1937, cannot benefit.

(The Commissioners appointed for the purposes of the Special Areas (Development and Improvement) Acts, 1934 and 1937, are empowered to grant assistance to a site company by way of a loan to induce the establishment of an industrial undertaking in the special areas.)

(3) THE BRITISH BROADCASTING CORPORATION  
(§ 19—1937).

In addition, such income of friendly societies, trades unions and charities as is exempted from Income Tax, is also exempted from N.D.C./P.T. (*see* Chapter IX, § 7). Interest from tax reserve certificates is exempted (§ 38—1942).

(4) The exemption from P.T. of sole traders and partnerships involves the determination of the N.D.C. liability thereon as if the years of charge to N.D.C. had ended at the end of 1946.

Personal representatives of a deceased person (including a body corporate acting as such representative) are not liable to P.T. in that capacity (§ 31—1947). If the business of a company is carried on by a liquidator, trustee, etc., it will be regarded as carried on by the company, although the liquidator, etc., will be liable to be assessed and must make returns, etc., (§ 44—1947).

(5) Should the income of a controlled company be apportioned by a direction under § 21, 1922, for Sur-tax purposes (*see* Chap. VIII, § 7), P.T. is not chargeable on the profits if all the persons to whom it is apportioned are individuals. This applies to any chargeable accounting period if the apportionment is made for a year or period which includes (or for years or periods which include) the whole of the chargeable accounting period.

If all the persons to whom the income is so apportioned are not individuals, notice may be given to the C.I.R. within six months after the end of the chargeable accounting period (or such longer time as the C.I.R. may allow), by the persons who are not individuals,



electing that the income in question shall be charged to P.T. as if they were carrying on a business in partnership (liable to P.T.) and the share of each of the profits or losses of the business of such partnership were equal to the income apportioned to the person in question, and as if any payment received from the company the profits of which were apportioned other than a payment allowable in computing that company's profits) had not been made. The controlled company will not then be liable to P.T.

In the above references to apportionment, the provisions regarding sub-apportionment have effect, with the result that it is only the persons to whom the profits are ultimately apportioned that are taken into account (§ 31—1947).

#### Illustration.

A.B. Ltd. is a controlled company, and a direction is made under § 21, 1922. If the profits are wholly apportioned and sub-apportioned to individuals, A.B. Ltd. is exempted from P.T. thereon.

If, however, part of the profits are ultimately apportioned to C.D. Ltd. and E.F. Ltd., these three companies, A.B. Ltd., C.D. Ltd. and E.F. Ltd. may give notice requiring P.T. to be assessed as if the business had been carried on by C.D. Ltd. and E.F. Ltd. in partnership. The effect appears to be that C.D. Ltd.'s apportioned share will be added to its income, and that of E.F. Ltd. added to its income. Any dividends received from A.B. Ltd. will be excluded from the income of C.D. Ltd. and E.F. Ltd. A.B. Ltd. will not be liable to P.T.

The above provisions apply to each chargeable accounting period, the whole of which is included in a year or period or years or periods for which the income is apportioned (§ 31—1947).

If such notice is not given, it seems that P.T. will be payable on the whole of the profits of the controlled company, notwithstanding that part has been apportioned to individuals.

#### § 4.—Computation of Profits.

As already stated, the profits arising from a trade or business in each chargeable accounting period are to be separately computed on the principles on which profits are computed for the purpose of Income Tax under Case I of Schedule D, with certain modifications dealt with in § 8 hereunder.

In the case of investment and similar companies which are not assessable to Income Tax under Case I, the profits are to be computed as if they were so assessable (§ 20—1937).

#### § 5.—Accounting Periods.

Accounting periods of a trade or business are determined as follows:—

- (a) in a case where the accounts of the trade or business are made up for successive periods of twelve months, each of those periods shall be an accounting period ;
- (b) in a case where the accounts of the trade or business have previously been made up for periods of twelve months but have ceased to be so made up, the accounting periods from the end of the last period of twelve months for which they were so made up shall be such periods not exceeding twelve months as the Commissioners of Inland Revenue may determine ;
- (c) in any other case, the accounting periods of a trade or business shall be such periods not exceeding twelve months as the Commissioners of Inland Revenue may determine.

The expression “ chargeable accounting period ” means—

- (i) any accounting period determined as above which falls wholly within the five years beginning on the 1st April, 1937 ; and
- (ii) in a case where any such accounting period overlaps the beginning or end of the said five years, such part of that period as falls within those five years.

Where a chargeable accounting period is not a period for which the accounts of the trade or business

have been made up, the profits and losses for any period for which accounts have been made up are to be apportioned to arrive at the profits arising in the chargeable accounting period.

Any such apportionment is made in proportion to the number of months or fractions of months in the respective periods, unless the Commissioners of Inland Revenue, having regard to any special circumstances, otherwise direct (§ 20—1937).

The distinction between “accounting period” and “chargeable accounting period” is important. “Accounting period” means the period of account the profits of which are adjusted for N.D.C. purposes, whether they fall wholly within the period of charge or not.

The “chargeable accounting periods” are the accounting periods (arrived at as above) that fall wholly after 31st March, 1937, and such part of any overlapping accounting period as falls after that date.

#### Illustration.

The accounts of a business are made up consistently for years ending 31st December.

The accounting periods are therefore years ending 31st December.		The chargeable accounting periods are—	
1937	..	Nine months to	31st December, 1937
1938	..	Year to	31st December, 1938
1939	..	Year to	31st December, 1939
1940	..	Year to	31st December, 1940
1941	..	Year to	31st December, 1941
1942	..	Year to	31st December, 1942
1943	..	Year to	31st December, 1943
and so on.			

The profits of an underwriting agent are profits of the year in which the work is done (*Gardner, Mountain v. D'ambrumenil* (1946), T.R. 149)

The abbreviation "C.A.P." will now be used to designate "chargeable accounting period." Normally, the accounting period will be recognised as the C.A.P., unless there is an overlap of, or a gap between, accounting periods. If an accounting period exceeds a year, it will usually be divided into two C.A.P.'s, one of a year and the other of the balance of the period. Where businesses separately assessed for N.D.C. became assessed as one business for P.T., and the accounting periods do not coincide, the following provisions apply (§ 43—1947):—

- (a) The parts of the said periods that fall before the end of 1946 are to be treated for the purposes of P.T. as separate accounting periods; and
- (b) Accounting periods (the first of which begins on 1st January, 1947) shall be determined as if the combined business had commenced on 1st January, 1947; and
- (c) The combination of businesses shall not apply to (a) but shall apply to (b).

### § 6.—Adjustment of Profits.

The assessments to N.D.C./P.T. are made on the actual adjusted profits of accounting periods, not, like Income Tax, by reference to basic years (4th Sch., R. 1—1937). The accounts are to be adjusted by reference to the Income Tax law in force for the year of assessment in which the chargeable accounting period ends (§ 43—1941).

The modifications of the Income Tax Rules as applied to N.D.C./P.T. are as follows:—

#### (a) Annual Payments and Rent.

The principles of the Income Tax Acts under which deductions are not allowed for interest, annuities or

other annual payments payable out of the profits, or for royalties, or (in certain cases) for rent (*e.g.*, mineral rents), and under which the annual value of lands, etc., occupied for the purpose of a trade or business is excluded, and under which a deduction may be allowed in respect of such annual value, are not to be followed.

Nothing in this paragraph, however, is to authorise any deduction in respect of—

- (a) any payment of dividend or distribution of profits ; or
- (b) any interest, annuity or other annual payment paid to any person carrying on the trade or business, or any royalty or rent so paid. For this purpose, where the trade or business is carried on by a company the directors whereof have a controlling interest therein, the directors, *other than whole-time service directors*, are deemed to be carrying on the trade or business (4th Sch. R. 4—1937; 8th Sch., Pt. III, R. 1—1947).

N.B.—The words in italics apply to P.T. only ; they did not apply to N.D.C.

For Income Tax purposes, annual payments have to be “ added back ” to profit because of the principle of assessment at the source. This is unnecessary for N.D.C./P.T., and so long as the annual payment is wholly paid out in earning the profits, it is a proper deduction in adjusting accounts for N.D.C. except as stated in (b) below (§ 14—No. 2 1940). Where premises are owned or beneficially occupied for the purposes of the business, the annual value is deductible for Income Tax purposes in lieu of rent, in order to avoid double taxation. This again is unnecessary for N.D.C./P.T., and no such deduction can be made.

**(b) Payments to Partners, etc.**

Annual payments, royalties or rents in the nature of an annual payment (*e.g.*, a ground rent) paid to a person carrying on the business cannot be deducted. The directors, *other than whole-time service directors (from 1st January, 1947)*, of a company are deemed to be persons carrying on the business where they have a controlling interest in the company. This provision was essential to stop up an obvious loophole. It is of the utmost importance to note, however, that this rule does not affect a rent *bonâ fide* paid for business premises provided it is allowed as a deduction for Income Tax purposes. All that the restriction does, is to prevent the allowance for N.D.C. purposes of rent which is disallowed for Income Tax.

**(c) Depreciation of Factories.**

The mills, factories allowance is deductible where appropriate, although the net annual value cannot be deducted.

**(d) Exceptional Depreciation of Buildings, Plant, etc.**

The allowance is provided from 1st April, 1939 to 31st December 1946 (*see* Chap. IV, §3 (*b*) for details).

**(e) Dominion Income Tax, etc.**

For Income Tax purposes, in view of the Dominion Income Tax relief given by reduction of the Income Tax payable in the United Kingdom, no deduction in the accounts is permissible for Income Tax payable in the Dominions. For N.D.C./P.T. purposes, however, any Income Tax payable in the Dominions in respect of the profits included in the accounts is allowed as an expense, just as Income Tax so paid in foreign countries is allowed (4th Sch., R. 6—1937).

Where relief from double taxation is given under arrangements with other Governments in respect of the profits from shipping, air transport and certain agencies, such profits are exempted from N.D.C./P.T. so long as the foreign Government's relief extends to all taxes (*ibid.*). (See also Appendix XVI. dealing with those cases where Double Taxation Relief Agreements are in force.)

**(f) United Kingdom Income Tax, Sur-Tax, Excess Profits Tax, N.D.C. or P.T.**

These are not allowed as deductions (4th Sch., R. 9—1937). Nor is interest on arrears of such taxes (§ 8—(No. 2) 1947).

**(g) Artificial Transactions.**

No deduction can be made in respect of any transaction or operation of any nature if and so far as it appears that the transaction or operation has artificially reduced the profits or created or increased a loss, or would artificially reduce the profits or create or increase a loss (4th Sch., R. 10—1937).

**(h) (i) Income from Investments or other Property up to 31st December, 1946.**

For the purposes of N.D.C. the income from outside investments of manufacturing and similar industries and of ordinary trading concerns was not taxable; it is not a trading receipt. Where investments are an essential element of the business, however, the interest thereon is part of the trading profit. Income received from investments or other property was therefore included in the profits in the case of the business of a building society, or a banking business, assurance business or business consisting wholly or mainly in the dealing in or holding of investments or other property,

but not otherwise. In these cases, the profits included all income received from investments or other property *except*—

- (i) income received directly or indirectly by way of dividend or distribution of profits from a body corporate carrying on a trade or business which was itself a business subject to N.D.C. (even if it did not pay N.D.C. owing to its profits being less than £2,000); and
- (ii) income to which the persons carrying on the trade or business are not beneficially entitled (4th Sch., R. 7).

For chargeable accounting periods, in-so-far as they fall after 31st March, 1939, and before 1st January, 1947, in the case of a business part of which consists in banking, assurance or *dealing* in (NOT holding) investments or other property, the profits must include all income received from investments or other property held for the purposes of that part of that trade or business, except (a) dividends, etc., from companies themselves within the National Defence Contribution charging section, and (b) income to which the persons carrying on the business are not beneficially entitled (§ 14—(No. 2) 1940).

Bank interest is income from investments (*C.I.R. v. Imperial Tobacco Co.* (1940), T.R. 375).

Royalties from a licence granted to another company for the purpose of forwarding the grantor's business are investment income (*C.I.R. v. Rolls Royce* (1941), T.R. 213).

In the cases of companies formed to hold blocks of flats or chambers or business premises and carrying



on the business of letting them for profit, the rents (not the Schedule A values) less expenses, are the profits for N.D.C. purposes. The income of a private landowner from his property is not taxable, but if he forms a private company, as is often done, for the purpose of carrying on the landholding and letting the land, the company will be liable.

Dividends received from companies which are themselves liable to N.D.C. are not to be included in the profits of the recipients, but investment and similar companies must include in their profits any debenture or other interest received from such companies, as well as interest on gilt-edged securities and other investments.

The underlying idea is to avoid taxing profits twice. Dividends are paid out of profits which have borne N.D.C. already, but interest paid has not borne N.D.C. as it is allowed as a deduction in arriving at the profits of the company which pays it.

Although, except in the cases already mentioned, investment income is to be excluded from profits, it should be noted that there is no provision for excluding any expenses in connection with such income. So long as such expenses are laid out wholly and exclusively for the purposes of the trade or business, they are allowable deductions. The rules of Case 1 will determine their admissibility. In an Income Tax case, where certain investment income had to be omitted as exempt, Lord Thankerton, in delivering a unanimous judgment of the House of Lords, said: " . . . . the investments in question were part of the business of the respondent's trade, and . . . . the expense connected with them was wholly or exclusively

laid out for the purposes of the trade. Expenditure in course of the trade which is unremunerative is none the less a proper deduction, if wholly and exclusively made for the purposes of the trade. It does not require the presence of a receipt on the credit side to justify the deduction of an expense" (*Hughes v. Bank of New Zealand* (1938), 11 A.T.C. at p. 145). As a result of this case, it is provided that, as from 1st April, 1939, where interest from tax-free Treasury securities is excluded owing to the person carrying on a business not being domiciled or ordinarily resident, any interest on money borrowed for the purpose of acquiring the securities, any other expenses attributable to the acquisition or holding of, or to any transaction in, the securities, and any profits or losses so attributable, must also be left out of account in computing profits (§ 14—(No. 2) 1940).

(ii) **Income from Investments, etc., after 31st December, 1946.**

For the purposes of P.T., the whole scheme of things is changed. The term "franked investment income" (abbreviated hereafter to "F.I.I.") is applied to income received directly by way of dividend or distribution of profits from a body corporate carrying on a business which is within the charge to P.T., and income so received from any other body corporate, being income received indirectly by way of dividend or distribution of profits from a body corporate carrying on a business within the charge to P.T.

All income received from investments or other property must be included in the profits for P.T. except—

(a) Franked investment income; and

- (b) income to which the person carrying on the trade or business is not beneficially entitled.

The profits of a body corporate which either alone or in conjunction with any statutory undertakers exempted from P.T. has a controlling interest in another exempt statutory undertaker, are not to include any income from the latter (§ 32—1947, amending R. 7 of 4th Sch. 1937).

**(i) Work in Progress.**

Where the performance of a contract extends beyond the chargeable accounting period, there must (unless the Commissioners of Inland Revenue owing to any special circumstances otherwise direct) be attributed to that period such proportion of the entire profit or loss which has resulted, or which it is estimated will result, from the complete performance of the contract as is properly attributable to that period, having regard to the extent to which the contract was performed in that period (4th Sch., R. 14—1937).

This provision ensures that work in progress shall be brought into account at a valuation that includes a fair proportion of the profit expected on the contract when completed. In some cases it can be agreed to defer adjustments until the contract is completed and the true result ascertained, when the profit or loss can be spread over the years during which the work was done.

- (j) **Payments into War Risks Pools** (now abolished) are not allowable deductions (§ 14—(No. 2) 1940).

**(k) Concentration of Industry (§§ 37, 43—1941).**

Any sum payable by one party to another under an arrangement for the concentration of industry or

business will be regarded as a trade expense and a trade receipt respectively, unless it is a capital sum or interest or other consideration for the use of borrowed money. A business will not be deemed to have ceased or changed because of any such arrangement. Any sum payable to a partner will be deemed to have been received by the partnership and distributed as a share of profits. Similarly, any sum paid direct to a director of a director controlled company will be deemed to have been received by the company and paid to him as remuneration.

**(l) Payments for war injuries to employees.**

As for income tax, these are disallowed (§ 43—1941).

**(m) Miscellaneous.**

In the case of schemes certified by the Board of Trade after 31st December, 1945, under § 25, 1935, contributions and payments under redundancy schemes are not to be taken into account in arriving at profits for N.D.C. (§ 34—(No. 2) 1945), but are to be taken into account for P.T. (§ 74 and 11th Sch., Part III, 1947). The same applies to schemes for the elimination or reduction of redundant works, machinery, etc., to which effect is given under any Act (*ibid.*) The Income Tax provisions for relief for Research Expenditure do not apply for N.D.C. (§ 36—(No. 2) 1945), but apply for P.T. (§ 46 and 8th Sch., Part I, R. 5, 1947).

The following are allowable as deductions in computing profits for P.T. but not for N.D.C.

- (a) Expenditure on additions or improvements to farm houses, farm buildings and cottages owned and forming part of the business assets, provided no increased rent is payable and the work is done to comply with statutory or local

authority requirements (cf. Rule 8, No. V, Schedule A, as amended by § 25, F.A., 1924, allowing such expenditure in maintenance claims) (Para. 3, Pt. III, 8th Schedule—1947).

- (b) Mineral rights duty or royalties welfare duty (Para. 4, *ibid*).

The provisions *re* valuation of farm animals, etc. (*see* Chap. VI § 6), are applicable for P.T. (§ 67 and 10th Sch.).

The deduction allowable for income tax in respect of payments for technical education (§ 29—1946) are not allowable for N.D.C. (§ 45—1946), but are allowable for P.T. (§ 74 and 8th Sch. Pt. 1, R. 5, 1947).

## § 7.—Wear and Tear and Obsolescence.

- (a) For N.D.C. to 31st December, 1946.

### (i) Current Wear and Tear.

An allowance for Wear and Tear of machinery and plant can be claimed in similar circumstances to the allowance for Income Tax purposes. For N.D.C., however, the Wear and Tear allowance for the accounting period is to be debited as an expense in the accounts (4th Sch., R. 3—1937). If, therefore, the allowance exceeds the profits which would otherwise result, there is no question of carrying forward the balance as Wear and Tear allowance; the resulting loss will be available for carry forward as a loss (*see* § 12 hereunder). The increase in the additional allowance from one-tenth to one-fifth operates from 1st April, 1938 (§ 44—1938), to 31st December, 1946 (§ 63—Income Tax Act, 1945, § 46 and 8th Sch.—1947).

The Revenue evolved a formula for computing Wear and Tear allowances, designed to allow Wear and Tear on additions from the time they are made. This formula is as follows:—

(i) *Businesses in existence before 1st April, 1937—*

To the written down value of the plant, etc., for Income Tax purposes at 5th April, 1937, add back such proportion of the Wear and Tear allowance for 1936-37 as is necessary to find the written down value of the plant at the commencement of the first accounting period, e.g.—

Written down value for Income Tax purposes, 5th April, 1937 .. .. .	£40,000
Allowance, 1936-37, £4,200	
Beginning of First Accounting Period, 1st January, 1937.	
Add $\frac{1}{3}$ ths of £4,200 .. .. .	1,050
Written down value, 1st January, 1937 .. .. .	<u>£41,050</u>

Compute Wear and Tear allowance for the accounting period on this opening figure and give proportionate relief on additions made during the accounting period.

Where the accounting period ends on 31st March, the written down value at 31st March, 1937, will be taken as the commencing figure on which to compute allowances for N.D.C. purposes.

(ii) *Businesses commenced after 31st March, 1937—*

Compute Wear and Tear allowance on the actual plant, etc., in use during each accounting period, proportionately from the date of purchase.

**Illustration.**

Accounts to 31st December ; Wear and Tear Allowance at 5%.

Written down value of Plant, etc., for Income Tax

purposes at 5th April, 1936 .. .. £100,000

Allowance (Income Tax), 1936-37, 5% .. .. 5,000

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95,000

Additions, 1936 .. .. 20,000

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Written down value, 5th April, 1937 .. .. 115,000

Add  $\frac{3}{12}$ ths of £5,000 .. .. 1,250

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Written down value, 1st January, 1937 .. .. 116,250

Allowance (N.D.C.), Accounting Period to 31st  
December, 1937, 5% .. .. 5,813

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110,437

Additions, 1937—

		Allowance	
		Months	Amount
31st March	£12,000	9	£450
30th June	10,000	6	250
31st October	6,000	2	50
	<u>£28,000</u>		<u>£750</u>

Additions, less Wear and Tear Allowances thereon 27,250

Written down value, 1st January, 1938 .. 137,687

Allowance (N.D.C.) (assuming that there were no  
further additions), 1938 .. .. 6,884

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Written down value, 1st January, 1939 .. £130,803

Wear and Tear Allowed—

Year to 31st December, 1937, £5,813 + £750 = £6,563

Add one-tenth .. .. 656

---

Total .. .. £7,219

Year to 31st December, 1938 .. .. £6,884

Add one-tenth for 3 months . . . £172

one-fifth for 9 months .. . 1,033

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1,205

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Total .. .. £8,089

It will be seen that where the formula is applied, the computations of Wear and Tear allowances for Income Tax and for N.D.C. will proceed along separate lines.

The application of the formula is so cumbersome in practice that in many cases, by agreement with the Inspector of Taxes, alternative methods are adopted, based on the allowances for Income Tax purposes. These are:—

- (a) To charge for Wear and Tear in the accounting period the agreed allowance for Income Tax purposes for the year of assessment in which the accounting period ends, *e.g.*, charge in the accounts for the year ended 31st December, 1938, the allowance for 1938-39.
- (b) To “split” the agreed allowances for Income Tax purposes over the accounting period, *e.g.*, charge in the accounts for the year ended 31st December, 1938, one quarter of the 1937-38 allowance (covering January to March, 1938) and three-quarters of the 1938-39 allowance (covering April to December, 1938).

Unless substantial sums have been spent in additions, it will be seen that the alternatives are much simpler to apply, without making any great difference to the amount allowed.

The Income Tax Act, 1945, did not apply for N.D.C. and wear and tear and obsolescence allowances continued on the old basis to 31st December, 1946. This meant that from 5th April, 1946, only one-fifth and not one-quarter of the allowance was added.



**(2) Pre-N.D.C. Wear and Tear.**

Allowance is also made for any unexhausted Wear and Tear allowances which were available for carry forward for Income Tax purposes when N.D.C. began. It is provided that any balance of Wear and Tear allowances brought forward for Income Tax purposes to be added to the allowance for 1937-38 is to be allowed for N.D.C. This "pre-N.D.C." Wear and Tear is not debited in the accounts, but is to be deducted from the profit of the first *chargeable accounting period*, and if it exceeds this profit, the balance is to be deducted from the profit of the next chargeable accounting period, and so on.

**Illustration.**

After assessing a trade to Income Tax for 1936-37, there remained a balance of Wear and Tear allowance amounting to £2,500 to be carried forward to 1937-38. This forms the pre-N.D.C. Wear and Tear for N.D.C. purposes.

The profits for the year to 31st December, 1937, adjusted for N.D.C. after deducting the current Wear and Tear allowance for that year, amounted to £3,000.

The first chargeable accounting period is from 1st April, 1937, to the 31st December, 1937, and the profits of that period are, therefore—

$\frac{9}{12}$ ths of £3,000	.. .. .	=	£2,250
From which is deductible the pre-N.D.C. Wear and			
Tear allowance of	.. .. .		2,500
Giving a nil profit and leaving pre-N.D.C. Wear			
and Tear allowance to carry forward of	..		<u>£250</u>

This will be deducted from the profits of 1938.

Had the first accounting period been the year to 31st March, 1938, the chargeable accounting period would have coincided, permitting the whole pre-N.D.C. Wear and Tear to be deducted at once.

**(3) Obsolescence.**

The obsolescence allowance is not mentioned in the Acts for N.D.C., and where the Wear and Tear allowance

is based on Income Tax figures, no adjustment is therefore necessary; the obsolescence allowed for Income Tax purposes is charged in the accounts according to Case I Rules, and is thus automatically allowed for N.D.C. Where the "formula method" is adopted, however, the obsolescence allowance must be re-computed, having regard to the Wear and Tear allowance made thereunder.

**(b) For P.T. after 31st December, 1946.**

For P.T., the special calculation of wear and tear allowances illustrated above is abolished. In all cases, it is necessary to apportion the allowances as agreed for Income Tax purposes. Where relevant, the obsolescence allowance will be that for Income Tax purposes (apportioned to fit the accounting period (R. 3, 8th Sch. Pt. I—1947). As for N.D.C., the wear and tear allowance is charged as an expense. Relief for pre-N.D.C. wear and tear not used continues.

**§ 8.—Allowances, etc., under the Income Tax Act, 1945 (8th Sch., Pt. I—1947).**

The following allowances did not apply to N.D.C., but they are applicable to P.T. as from 1st January, 1947, *viz.* :—

- (a) Wear and tear allowances at the amended rates;
- (b) initial, annual or balancing allowances under any provisions of the Act;
- (c) Allowances for capital expenditure on scientific research (§§ 28, 29 (1) (b), 2 (a)—1944);
- (d) allowances for capital expenditure on agricultural buildings, etc.

An allowance will be treated as related to the business if (a) it is made in charging the profits of the business, or (b) it is an allowance to a lessor for wear and tear, etc., under § 20, Income Tax Act, 1945, or an initial, annual or balancing allowance made by way of discharge or repayment of tax in respect of, or of expenditure on, property, the rent of which is included in the business profits of P.T., or would have been so included had there been any rent; or (c) it is an allowance under § 33, Income Tax Act, 1945, in respect of property used for the purposes of the business or the rent of which is or would be included in the profits.

The above allowances are apportioned to fit the accounting periods as already explained in connection with wear and tear.

A balancing charge under the 1945 Act, or a charge on capital sums received from the sale of patent rights, must similarly be included in the profits of the accounting period for Profits Tax, the figures for income tax years of assessment being apportioned to fit the accounting period. For this purpose, a charge will be treated as related to the business if it is made in charging the profits of a trade which is or is comprised in that business; or is a balancing charge in respect of (or of expenditure on) property the rent of which is included in the profits for Profits Tax (or would be included if there were any rent); or is a charge in connection with patent rights which have at any time been used for the purposes of the business.

Similar treatment is required in respect of any amount assessable to Income Tax on the sale of an asset in respect of which a scientific research allowance has been given.

**Illustration.**

The following are the Profit and Loss Accounts of A.B. & Co., Ltd. (a manufacturing company) for the years stated. Wear and Tear allowances have been agreed for Income Tax purposes at £600 for 1946-47, £560 for 1947-48, and £520 for 1948-49. The company owns a 999 years' lease of the factory, erected in 1920 at a cost (excluding land) of £8,500, assessed at £1,000 gross, and subject to a ground rent of £20. Compute the profits assessable to P.T., assuming the directors do not have a controlling interest in the company.

**PROFIT AND LOSS ACCOUNTS FOR YEARS****ENDED 31st DECEMBER.**

	1947. £	1948. £		1947. £	1948. £
To Trade Expenses	25,000	26,000	By Gross Profit ..	36,000	46,770
Ground Rent ..	20	20	Dividends on		
Income Tax ..	1,000	3,000	Investments	200	100
Directors' Fees	600	800	(All U.K.		
Debenture Interest ..	2,000	2,000	Trading		
Depreciation ..	1,800	1,700	companies.)		
Loss on Sale of					
Investments	—	300			
Bank Interest	100	50			
Reserve for P.T.	249	860			
Net Profit ..	5,431	12,140			
	<u>£36,200</u>	<u>£46,870</u>		<u>£36,200</u>	<u>£46,870</u>

**ADJUSTMENT OF PROFITS FOR PURPOSES OF P.T.**

		1947. £	1948. £
Net Profit per Accounts .. ..		5,431	12,140
Add Income Tax .. ..		1,000	3,000
Depreciation .. ..		1,800	1,700
Loss on Investments .. ..		—	300
P.T. .. ..		249	860
Carried forward ..		<u>£8,480</u>	<u>£18,000</u>

	Brought forward	..	£8,480	£18,000
<i>Deduct</i>	Annual Allowance	on		
	Factory	.. ..	£170	£170
	Wear and Tear Allowance	570	530	
		—	740	700
			7,740	17,300
	F.I.I.	.. ..	200	100
	Profits	.. ..	<u>£7,540</u>	<u>£17,200</u>

## NOTES :

(1) The Wear and Tear allowances are—

$$1947 \frac{1}{4} \text{ of } £600 + \frac{3}{4} \text{ of } £560 = £570.$$

$$1948 \frac{1}{4} \text{ of } £560 + \frac{3}{4} \text{ of } £520 = £530.$$

(2) The annual allowance for the premises is 2% on £8,500 = £170.

### § 9.—Limitation on Directors' Remuneration in the Case of Companies in which the Directors have a Controlling Interest.

In the case of a company controlled by the shareholders generally, the directors cannot be deemed to be in a position to fix their own fees. Where, however, the directors have a controlling interest in the company, they could normally draw out most or all of the profits as fees. To prevent the avoidance of N.D.C./P.T. by such an expedient, a limit is placed on the amount to be allowed for directors' remuneration, in the case of any company (within the meaning of the Companies Act, 1929, or the Companies Act (Northern Ireland), 1932) in which the directors have a controlling interest.

“Controlling interest” is not defined, and must therefore depend upon the facts of the case. Guidance is found in cases dealing with Excess Profits Duty,

etc. "The only interpretation that can be given to the expression 'controlling interest' is by reference to the power that the number of shares held gives to the holders to control the disposal of the company's assets and the administration of the company's affairs at a general meeting" (*Glasgow Expanded Metal Co. v. C.I.R.* (1923), 12 T.C. at p. 579). "A shareholder has a 'controlling interest' whose holding in the company is such that at a general meeting he is more powerful than all the other shareholders together" (*C.I.R. v. B. W. Noble* (1926), 12 T.C. at p. 926—a Corporation Profits Tax case). The control must be at a general meeting; the fact that the directors have power to issue to themselves unissued shares which would give them control is not relevant (*Himley Estates and Humble Investments v. C.I.R.* (1932), 17 T.C. 367). Directors who have a preponderance of voting power in companies which in turn control companies of which they are directors, have a controlling interest in the latter, even if they have no preponderance of voting power directly in them (*F. A. Clarke & Son v. C.I.R.*; *British-American Tobacco Co. v. C.I.R.* (1941), T.R. 129). Shares held as trustees must be included in determining whether the directors have control (*J. Bibby & Son v. C.I.R.* (1945), T.R. 171), though there is a doubt as to whether this applies to a bare trustee.

The term "director" has the same meaning as in Section 144, Companies Act, 1929 (*i.e.*, it includes a person in accordance with whose directions or instructions the directors are accustomed to act), with the addition that it includes any person who—

- (i) is a manager of the company or otherwise concerned in the management of the trade or business; *and*

- (ii) is remunerated out of the funds of the trade or business ; *and*
- (iii) is the beneficial owner of *not less than twenty per cent. of the ordinary share capital* of the company.

For this purpose, “ordinary share capital” is defined as all the issued share capital (by whatever name called) of the company, other than capital the holders whereof have a right to a dividend at a fixed rate or a rate fluctuating in accordance with the standard rate of Income Tax, but have no other right to share in the profits of the company. Participating preference shares are therefore deemed to be included in the “ordinary share capital.” A director who is required to devote substantially the whole of his time to the service of the company in a managerial or technical capacity and is *not the beneficial owner of more than five per cent. of the ordinary share capital* of the company is termed a “*whole-time service director*” (4th Sch., R. 13—1937).

Directors’ remuneration includes all remuneration paid or payable whether in respect of services as a director or otherwise, *including services of a secretarial managerial, advisory or technical nature* (§ 63—1947). This applies to N.D.C. and P.T. with the exception that if a taxpayer was successful in an appeal determined on or before 22nd January, 1947, whereby remuneration of a director for services in some office other than director was excluded from “directors’” remuneration, the effect of the appeal stands.

The following are, however, to be excluded from directors’ remuneration :—

- (a) If the director carries on a trade or profession assessable under Case 1 or Case 11 of Sch. D,

sums received (and included in such profits) for services rendered to the company in the course of his business ; and

- (b) If the director is a member of a profession and separately remunerated as an employee of the company, remuneration for services rendered in his professional capacity as a solicitor or accountant or services (not being secretarial or managerial in nature) not directly connected with the trade of the company, to the extent that the remuneration is reasonable and necessary (§ 63—1947).

Where a company in which the directors have a controlling interest carries on a trade or business in any chargeable accounting period, the deduction to be allowed in respect of the remuneration of directors, *other than whole-time service directors*, shall not exceed 15 per cent. of the profits arising from the business in the period (computed before deducting any remuneration of directors other than whole-time service directors), or £2,500 (prior to 1st January, 1947, £1,500), whichever is the greater, with a maximum deduction of £15,000. In a chargeable accounting period of less than twelve months, the proportionate part of £2,500 and £15,000 must be taken as the limit (4th Sch., R. 11—1937 ; § 45—1947).

It will be seen that, although whole-time service directors are taken into account in determining whether the directors have a controlling interest, their remuneration is not limited, and the maximum remuneration of the other directors (including managers who come within the definition) is calculated by reference to the profits after deducting the remuneration



of whole-time service directors. If the actual remuneration is less than the limit allowable, the actual amount is allowed. The limitation is on the total remuneration of all directors (other than whole-time service directors) not "per director."

In other words, where the profits of the year do not exceed £16,667 (before deducting remuneration of directors other than whole-time service directors) the maximum remuneration is £2,500; where such profits exceed £16,667 but not £100,000, the maximum is 15% of those profits; and where the said profits exceed £100,000, the maximum is £15,000. For N.D.C., the figures were: up to £10,000, £1,500; over £10,000 up to £100,000, 15 per cent., thereafter £15,000.

#### Illustration.

A company had the following issued share capital, all fully paid :—

	£1 6% First Preference Shares.	£1 5% free of tax Second Preference Shares.	Participating £1 4% Preference Shares entitled to a further 6% after the Ordinary shareholders have had 10%.	£1 Ordinary Shares.	1/- Deferred Shares entitled to half the profits after the Ordinary shareholders have had a dividend of 20%.
	No.	No.	No.	No.	No.
Held by					
Director A ..	10,000	—	—	15,000	10,000
Director B ..	—	—	3,000	10,000	10,000
Held by whole- time service					
Director C ..	10,000	3,000	2,000	1,000	2,000
Held by					
Manager D ..	—	2,000	1,000	14,000	1,500
Held by					
Manager E ..	—	—	—	1,000	5,000
Held by					
other persons	30,000	15,000	4,000	19,000	1,500
	50,000	20,000	10,000	60,000	30,000

None of the preference shares entitles the holder to vote, but each ordinary and deferred share carries one vote.

The "controlling interest" and "ordinary share capital" are therefore as follows:—

	Participating Preference Value.	Ordinary.		Deferred.		Total.	
		Votes.	Value.	Votes.	Value.	Votes.	Value.
Director							
A	—	15,000	£15,000	10,000	£500	25,000	£15,500
B	£3,000	10,000	10,000	10,000	500	20,000	13,500
C	2,000	1,000	1,000	2,000	100	3,000	3,100
Manager							
D	1,000	14,000	14,000	1,500	75	15,500	15,075
	£6,000	40,000	£40,000	23,500	£1,175	63,500	£47,175
E	—	1,000	1,000	5,000	250	6,000	1,250
Other persons	4,000	19,000	19,000	1,500	75	20,500	23,075
	£10,000	60,000	£60,000	30,000	£1,500	90,000	£71,500

Manager D holds "not less than 20%" of the ordinary share capital, since he holds £15,075 out of £71,500. He is, therefore, deemed to be a director.

C is a whole-time service director, since his holding does not exceed 5% of the ordinary share capital (£3,100 out of £71,500).

Both C and D must be considered as directors for the purposes of arriving at a controlling interest. The directors, therefore, control over half the votes at a general meeting, and have a controlling interest, so that their remuneration is restricted.

The remuneration voted was as follows:—

	Fees.	Salary.	Commission.	Total.
	£	£	£	£
A	2,000	—	—	2,000
B	2,000	—	—	2,000
C	500	1,000	300	1,800
D	—	1,500	1,000	2,500
E	—	800	400	1,200
	<u>£4,500</u>	<u>£3,300</u>	<u>£1,700</u>	<u>£9,500</u>

The company's adjusted profits for the year were £33,500 after charging the above amounts and Wear and Tear allowance for the year, but before adjusting for excess remuneration.

Show the final adjusted profits.

Profits as above	.. .. .	£33,500
Add Remuneration of A, B and D	..	6,500
		<hr/>
		40,000
Deduct Maximum remuneration, 15%	..	6,000
		<hr/>
Adjusted Profits	.. ..	<u>£34,000</u>

In the course of discussion of these provisions in Parliament, the Chancellor of the Exchequer stated that his advisers were "pretty confident that they would be able to secure that the real intentions were carried out, and that the device of putting shares in the hands of a nominee would not defeat those intentions." He went on to say: "Needless to say, and I hereby give public notice, if there was reason to think that the arrangement we are now making was being defeated by any such device, then I am quite certain Parliament would not be content, and we should have to take more active steps to stop it."

It will have been noted that where the directors have a controlling interest in the company, any annual payments made to directors other than whole-time service directors are disallowed as deductions, and only rents allowed in the Case I, Income Tax computation may be deducted, other rents paid to directors being disallowed.

### § 10.—Minimum Profits Exemption.

Where the profits arising in any chargeable accounting period from the trade or business do not exceed (before abatement) £2,000, no N.D.C./P.T. is payable thereon. If the chargeable accounting period is one of less than a year, the proportionate part of £2,000 is the limit for this purpose, *e.g.*, if the period is nine

months, the profits will be exempt if they do not exceed  $\frac{1}{5}$ ths of £2,000 = £1,500 (§ 21—1937). For P.T. franked investment income must be included in the profits for this purpose (as well as other investment income (§ 33—1947)), and it will be remembered that all businesses carried on by the same person are treated as one.

### § 11.—Abatement.

For N.D.C., where the profits arising in any chargeable accounting period from the trade or business exceed £2,000 but are less than £12,000, an abatement is allowed of a sum equal to one-fifth of the difference between the amount of the profits and £12,000. If the period is less than a year, the proportionate part of £2,000 and £12,000 must be taken (§ 21—1937). It will be seen that £12,000 per annum is £1,000 per month.

#### Illustration (1).

Chargeable Accounting period.	Adjusted Profits.	Abatement— 1/5th of	Net amount chargeable.	N.D.C. payable if business carried on by—		
				A Company or other Corporate body, 5%	An individual or partnership 4%	
months	£	£    £	£	£	£   s.   d.	
(a) 12	2,100	12,000 ~ 2,100	120	6	4   16   0	
(b) 12	5,000	12,000 ~ 5,000	3,600	180	144   0   0	
(c) 12	11,000	12,000 ~ 11,000	10,800	540	432   0   0	
(d) 12	13,000	nil	13,000	650	520   0   0	
(e) 9	6,000	9,000 ~ 6,000	5,400	270	216   0   0	
(f) 6	5,000	6,000 ~ 5,000	4,800	240	192   0   0	

For purposes of checking calculations, it is useful to note that the effect of the abatement is to charge 6 per cent. on the excess of the profits over £2,000 per annum in the case of companies, etc., and 4·8 per cent. in the case of sole traders and partnerships, *e.g.*, in the above illustration,

(a) 6% of (£2,100 — £2,000) = £6 ;

(c) 4·8% of (£11,000 — £2,000) = £432 ;

(f) 6% of (£5,000 — £1,000) = £240, and so on.

For P.T. (*i.e.*, from 1st January, 1947), where there is no franked investment income, abatement continues as before (save, of course, that investment income is included in the profits, and all businesses carried on by the same person are regarded as one unit instead of several units). If, however, there is franked investment income, the abatement is, in effect, apportioned partly to such income, *i.e.*, the abatement is such sum as bears to one-fifth of the amount by which the profits (computed before abatement but *including* franked investment income) fall short of £12,000, the same proportion as the said profits, *excluding* franked investment income, bear to the profits *including* franked investment income (§ 33—1947).

**Illustration (2).**

Trading profit .. .. .	£4,000
Investment Income (other than "franked")	2,000
Franked Investment Income .. ..	1,500
	<hr/>
	7,500
Deduct Franked Investment Income ..	1,500
	<hr/>
	6,000
Abatement—	
6,000      12,000—7,500	
<hr/>	
7,500      5	.. .. . 720
	<hr/>
	£5,280

P.T. payable 25% on £5,280, less 15% on the non-distributed proportion thereof.

[The apportionment of the abatement is revealed by the following :—

	Total Income	Income liable to P.T.	Franked Invest- ment Income not liable to P.T.
	£7,500	£6,000	£1,500
Abatement £ $\frac{12,000-7,500}{5}$ ..	900	720	180
	<hr/>	<hr/>	<hr/>
	£6,600	£5,280	£1,320 ]

Where the C.A.P. is less than a year, the £12,000 is, of course, diminished proportionately.

**§ 12.—Distributions.***(a) Definition.*

The term "distribution" means (§ 36—1947):—

- (a) any amount distributed directly or indirectly by way of dividend or cash bonus to any person; or
- (b) the value of any assets distributed in kind to any person; or
- (c) in the case of a director-controlled company, any amount applied, whether by way of remuneration, loans or otherwise, for the benefit of any person.

No sum applied in repaying a loan or in reducing share capital of the company carrying on the business is to be treated as a distribution.

Where income tax is deductible from a distribution, the gross amount representing income for the purposes of the Income Tax Acts, must be regarded as the amount of the distribution.

If a loan has been treated as a distribution for a C.A.P., and P.T. payable for that period has been increased as a result, and the loan is subsequently repaid, the C.A.P. in which it is repaid will reap the benefit in that the gross distributions for that period will be reduced by the sum tax on which at 15% would be equal to the increase. If the repayment takes place after the end of the last C.A.P. of the business, the distributions of the last C.A.P. will be reduced by the said sum. Any excess of the said sum over gross distributions of the C.A.P. will be carried forward. No provision is made for relief for excesses after the last C.A.P. If the C.A.P. differs from the accounting period, the usual apportionments apply. This does not necessarily give full relief as will be seen below in (c).

(b) *Gross Relevant Distributions to Proprietors* (§ 35—1947).

This term includes all distributions to members in so far as they are not allowable as deductions from profits for the purposes of P.T. A distribution is related to a C.A.P. as follows :—

- (a) A dividend declared not later than 6 months after the end of the period, but expressed to be paid in respect of the period (or part of it), will be regarded as a distribution in the C.A.P. for which it is paid.
- (b) Any other distributions (including dividends declared after the 6 months) will be regarded as distributions in the C.A.P. in which they are paid.
- (c) In the last C.A.P. in which a business is carried on, any distribution made after the end of that C.A.P. which is not a distribution of capital or a dividend under (a) above, will be regarded as a distribution in the last C.A.P. This does not apply, where the companies concerned give notice within 6 months (or extended time allowed by the C.I.R.), to shares issued as consideration on amalgamation or reconstruction, in which cases the company taking over the business succeeds to the rights, etc., of the vendors as to past non-distribution reliefs (§ 36—1947).

In (c), only repayments of (1) the total nominal amount of the paid up share capital, plus (2) any premiums received in cash thereon, are deemed to be distributions of capital.

For the purposes of (a) where a dividend could not reasonably have been declared within 6 months, the

C.I.R. may extend the time. A company can elect, by notice given to the C.I.R. before 1st February, 1948 (or such longer time as the C.I.R. allow), for the 6 months to be read as 9 months, or if the company carries on business or has interests abroad, 12 months.

To prevent avoidance of P.T., a transitional provision applies to dividends declared after 15th April, 1947, in respect of a C.A.P. or part of a C.A.P. which falls before 1st January, 1947. If the total of the dividends expressed to be paid in respect of (or of any part of) such a period, exceed the total of the dividends in respect of the immediately preceding C.A.P., the excess is to be treated as a distribution of the C.A.P. in which it is paid. If, however, the share capital has been increased, the company can elect to be treated as if the dividends of the preceding C.A.P. were correspondingly increased. Likewise, where the preceding C.A.P. and the succeeding C.A.P. are not of the same length, the dividends for the preceding period are to be correspondingly increased or reduced.

The term "dividend" includes an interim dividend. A dividend is treated as declared—

- (a) if declared in general meeting, on the date of declaration ;
- (b) in any other case, when it is paid, save that—
  - (i) if a dividend declared at a general meeting is in accordance with a directors' recommendation publicly announced at an earlier date, that date must be taken ; and
  - (ii) if a dividend is declared as a result of a decision of the directors and they publicly announce it, the date of announcement may be taken if the company elects (§ 35—1947).



Where a C.A.P. is not a period for which the accounts have been made up, the gross relevant distributions are computed as if the periods for which the accounts were made up were C.A.P's., and such division and apportionment (in months and fractions of months) to specific periods shall be made as appears necessary to arrive at the gross relevant distributions for the C.A.P. (§ 34—1947).

(c) *Net Relevant Distributions to Proprietors* (§ 34—1947).

These are the proportion of the Gross Relevant Distributions for the C.A.P. that the profits for the period bear to the profits computed before abatement and including franked investment income.

If the gross relevant distributions exceed the profits (computed without abatement and including franked investment income), the net relevant distributions are the sum of—

- (a) the profits (abated where relevant and excluding franked investment income), and
- (b) the excess of the gross relevant distributions over the profits computed without abatement and including franked investment income.

**Illustration (1).**

Profits (excluding franked investment income) after all adjustments except directors' remuneration	£20,000
Add Directors' Remuneration charged in Accounts	5,000
	<hr/> 25,000
Deduct Directors' Remuneration allowable 15% ..	3,750
	<hr/> £21,250
Profits excluding franked investment income ..	£21,250
Franked investment income .. ..	8,000
	<hr/>
Profits including franked investment income ..	<u>£29,250</u>

## Gross Relevant Distributions—

Dividends .. .. .	£4,000
Directors' remuneration disallowed ..	1,250
	<u>£5,250</u>

## Net Relevant Distribution—

21,250	
<u>29,250</u> × £5,250 .. .	£3,814
P.T. payable 25% on £21,250 ..	£5,312 10 0
Less 15% on £21,250 – 3,814 ..	2,615 8 0
	<u>£2,697 2 0</u>
Being 10% on £21,250 ..	£2,125 0 0
Plus 15% on £3,814 ..	572 2 0
	<u>£2,697 2 0</u>

The effect of the abatement is shown in the following illustration :—

## Illustration (2).

Profits, before adjusting directors' remuneration ..	£5,500
Add Directors' Remuneration .. .. .	6,000
	<u>11,500</u>
Deduct Franked Investment Income .. .. .	3,000
	<u>8,500</u>
Deduct Directors' Remuneration allowable .. ..	2,500
	<u>£6,000</u>
Abatement—	
6,000    £12,000 – 9,000	
<u>9,000</u> ×                      5 .. .. .	400
	<u>£5,600</u>

The profits computed without abatement and including franked investment income are £6,000 + £3,000 = £9,000.

Gross Distributions (including £3,500 directors' fees disallowed) .. .. .

5,600		<u>£6,300</u>
Net Distributions ——— × £6,300 .. ..		<u>£3,920</u>
9,000		
P.T. 10% on £5,600 .. ..	£560 0 0	
15% on £3,920 .. ..	588 0 0	
	<u>£1,148 0 0</u>	

**Illustration (3).**

In Illustration (2) had the gross relevant distribution been £10,000, the net relevant distributions would have been—

Gross distribution	..	..	..	..	£10,000
Less Profits, before abatement and including franked investment income	..	..	..	..	9,000
					<hr/>
Excess	..	..	..	..	1,000
Profits	..	..	..	..	5,600
					<hr/>
Net distribution	..	..	..	..	<u>£6,600</u>
					<hr/>
P.T. 25% on £5,600	..	..	..	£1,400	0 0
15% on £1,000	..	..	..	150	0 0*
					<hr/>
				<u>£1,550</u>	<u>0 0</u>

\* Subject to reduction by the amount by which the total non-distribution relief for all previous C.A.P.'s falls short of £150.

It will be seen that, as with abatement, the principle is to regard the gross distribution as paid proportionately out of the profits liable to Profits Tax and those which escape.

**Illustration (4).**

	Profits including F.I.I.	Profits excluding F.I.I. (after abatement)	Profits escaping P.T., i.e. F.I.I. and amount of abatement.
Based on previous illustration (2)	£9,000	£5,600	£3,400
The gross distribution is deemed to be made thus :	.. .. 6,300	3,920	2,380
	<hr/>	<hr/>	<hr/>
	<u>£2,700</u>	<u>£1,680</u>	<u>£1,020</u>

		£	s.	d.
Profits Tax : 25% on £5,600	..	1,400	0	0
Less : non-distribution relief :				
15% on £1,680	.. ..	252	0	0
		<hr/>		
		<u>£1,148</u>	<u>0</u>	<u>0</u>

Based on illustration (3)	..	£9,000	£5,600	£3,400
Gross distribution	..	10,000	<u>5,600</u>	<u>3,400</u>
Excess	..	<u>£1,000</u>		

		£	s.	d.
Profits Tax : 25% on £5,600	..	1,400	0	0
15% on £1,000	..	150	0	0*
		<u>£1,550</u>	<u>0</u>	<u>0</u>

\* Limited to past non-distribution relief.

The distribution charge on the amount by which the gross distribution exceeds the profits (including franked investment income and before abatement), cannot exceed the amounts on which non-distribution relief has been given in the past (§ 30 (2), proviso-1947). Non-distribution relief for a C.A.P. that bridges 31st December, 1946, is reduced by the amount apportionable to that part of the C.A.P. which fell before that date (§ 47 (4)—1947).

#### Illustration (5).

		1947	1948	1949
Profits	..	£20,000	£25,000	£18,000
F.I.I.	..	5,000	5,000	6,000
		<u>15,000</u>	<u>20,000</u>	<u>12,000</u>
Gross distribution	..	<u>£12,000</u>	<u>£19,000</u>	<u>£29,000</u>
		1947	1948	1949
Profits liable to P.T.	..	(a) £15,000	(a) £20,000	(a) £12,000
Net distribution :				
15,000				
<u>      </u> × £12,000	=	9,000		
20,000				
<u>      </u> × £19,000	=		15,200	
25,000				
£12,000 + (29,000 - 18,000) =				(c) 23,000
		<u>(b) £6,000</u>	<u>(b) £4,800</u>	<u>Nil</u>

Profits Tax : 25% on (a)	£3,750	£5,000	£3,000
Less : 15% on (b) ..	900	720	
Plus 15% on (c), but limited to 15% on (b) for 1947 and 1948 ..			1,620
(d) Profits Tax payable	<u>£2,850</u>	<u>£4,280</u>	<u>£4,620</u>

The profits for the three years are—

$$£15,000 + £20,000 + £12,000 = £47,000.$$

As these have all been distributed by the end of 1949, they are liable to P.T. at 25%, *i.e.*, the P.T. is £11,750, which is the total of (d) above. The excess of the gross distribution over the total profits in 1949 is £11,000, but only £10,800 has come out of previous profits on which non-distribution relief has been given. The balance must have come out of profits made before P.T. operated, and the Act does not extend to tax it.

#### Illustration (6).

The following illustration shows the position where loans to directors of a director-controlled company are repaid :—

	Year	1	2
Total Profits .. .. .		£20,000	£13,000
Add : Directors' remuneration		4,000	3,000
		<u>24,000</u>	<u>16,000</u>
Deduct : F.I.I. .. .. .		2,000	1,000
		<u>22,000</u>	<u>15,000</u>
Directors' remuneration allowable		3,300	2,500
		<u>18,700</u>	<u>12,500</u>
Profits for P.T. .. .. .		18,700	12,500
Add : F.I.I. .. .. .		2,000	1,000
		<u>£20,700</u>	<u>£13,500</u>
	Year	1	2
Gross Distribution :			
Dividends .. .. .		£12,000	£8,000
Directors' remuneration disallowed		700	500
Directors' loans .. .. .		5,000	—
		<u>£17,700</u>	c/f. <u>£8,500</u>

				Brought forward ..	£8,500
Less : *re loans repaid					
	18,700				4,517
	<u>20,700</u>	× £5,000	.. ..		<u>£3,983</u>
Net Distribution :					
	18,700				
	<u>20,700</u>	× £17,700	.. =	<u>£15,990</u>	
	12,500				
	<u>13,500</u>	× £3,983	.. ..		<u>£3,688</u>

\*The Act does not give full relief for the loans repaid. It says: "Where a loan has been treated as part of the gross relevant distributions . . . for a C.A.P., and as a result, the amount of tax payable for that period has been increased . . . the gross relevant distributions . . . for the period in which repayment is made . . . shall be treated as reduced by . . . the amount tax on which at 15 per cent. would be equal to the increase." In year 1, tax was increased by  $\frac{18,700}{20,700} \times £5,000 = £4,517$  at 15% as a result of the loans, and it is this amount that is to be deducted from the *gross* distribution of year 2.

This does not give full relief; the deductions ought to be from the net distribution. It is to be hoped that this will be amended.

#### (d) Transitional Provisions.

If a C.A.P. bridges 1st January, 1947, it is necessary to compute the N.D.C. to 31st December, 1946, on the old basis, and the P.T. thereafter on the new one. The Act requires the computations to be made for the whole C.A.P. and the results apportioned in months and fractions of months, unless apportioned on some other basis for E.P.T., when the same basis shall be adopted; this will arise quite frequently, *e.g.* (where a special account has been prepared for E.P.T. to 31st December, 1946) (§ 47—1947).

A change in the ownership of a business will be regarded as the cessation of the business and the commencement of a new one (§ 43—1947).

#### Illustration.

Director-controlled company, paying no dividends.  
Year ended 30th September, 1947.

	N.D.C.	P.T.
Profits as for Income Tax (before	£	£
deducting N.D.C. or P.T.)	11,000	11,000
N.A.V. .. ..	450	450
Directors' Remuneration ..	3,000	3,000
Carried forward ..	<u>£14,450</u>	<u>£14,450</u>

	Brought forward ..	£14,450	£14,450
Interest received .. ..	..	..	450
Franked Investment Income ..	..	..	500
Other Investment Income ..	..	..	400
Loan Interest paid <i>other than to</i> <i>directors</i> .. ..	£1,400	£1,400	
Loan Interest paid to whole time service directors .. ..	—	200	
Ground Rent .. ..	100	100	
Wear and Tear, etc. .. ..	1,450	1,600	
		<u>14,450</u>	<u>15,800</u>
		<u>2,950</u>	<u>3,300</u>
		11,500	12,500
Directors' Remuneration ..	1,500	2,500	
		<u>10,000</u>	<u>10,000</u>
Franked Investment Income ..			500
			<u>9,500</u>
Abatement— £12,000—10,000 .. ..	400		
<u>5</u>			
9,500	£12,000—10,000 ..		
<u>10,000</u> × <u>5</u>			380
Profits subject to P.T. .. ..	£9,600	£9,120	
	N.D.C.	P.T.	
	£ s. d.	£ s. d.	
5% on £9,600 .. ..	480 0 0		
25% on £9,120 .. ..		2,280 0 0	
Less : Non-distribution relief— Profits .. ..	£9,120		
Net Distribution (Directors' Re- muneration) :			
9,120			
<u>10,000</u> × £500	456		
15% on	<u>£8,664</u>	1,299 12 0	
	<u>£480 0 0</u>	<u>£980 8 0</u>	

	£	s.	d.
Being 10% on £9,120 ..	912	0	0
15% on £456 .. ..	68	8	0
	<u>£980</u>	<u>8</u>	<u>0</u>
P.T. payable $\frac{1}{4} \times £480 + \frac{3}{4} \times £980$ 8 0 =	<u>£855</u>	<u>6</u>	<u>0</u>

If the company was subject to Excess Profits Tax for the period ended 31st December, 1946, the proportion of the above tax applicable to the 3 months to 31st December, 1946, would not be payable.

(e) *Non-residents* (§ 39—1947).

The profits of a person who is ordinarily resident outside the United Kingdom for the whole of the C.A.P., are to be computed as if no net relevant distributions have been made, *i.e.*, Profits Tax will be charged at 10%.

Where a company not ordinarily resident in the United Kingdom controls directly or indirectly for the whole C.A.P., not less than one half of the voting power of a company ordinarily resident in the United Kingdom, distributions to the former company are to be left out of account in computing the latter's net relevant distributions. If the franked investment income of a company includes income received from a non-resident company to which this section applies, distributions are to be determined as if the profits included such income (this does not extend to profits to be taken "without abatement and including franked investment income," *i.e.*, the income received from the non-resident company is added to the assessable profits only).



### § 13.—Remuneration of Sole Traders and Partners (N.D.C. only).

In the case of a business carried on in any chargeable accounting period by an individual or by individuals in partnership, a claim could be made by him or them to be allowed the maximum deduction for remuneration that a company in which the directors have a controlling interest could be allowed in respect of directors other than whole-time service directors. The N.D.C. was then charged at 5% instead of 4% (4th Sch., R. 12—1937). The claim had to be made in writing within six months after the end of the chargeable accounting period in question, or such longer time as the Commissioners of Inland Revenue in any case allowed (§ 46—1938).

This provision was necessary in order to prevent a sole trader or partnership from having to pay a larger amount in N.D.C. than a company would have had to pay on the same profits.

Unless there were losses or pre-N.D.C. Wear and Tear allowances brought forward, the claim was not beneficial unless the profits were under £9,500 for the year, but where there were such reliefs to bring forward, each case had to be computed on its merits.

#### Illustrations.

(i) Where remuneration is not claimed—

BUSINESS.			
	(a)	(b)	(c)
Profits for year ..	£7,000	£10,000	£40,000
Less Losses and pre-N.D.C. Wear and Tear brought forward ..			26,000
Abatement ..	1,000	400	—
	<u>£6,000</u>	<u>£9,600</u>	<u>£14,000</u>
N.D.C. at 4% ..	<u>£240</u>	<u>£384</u>	<u>£560</u>

(ii) Where remuneration is claimed—

Profits for year ..	£7,000	£10,000	£40,000
Less Remuneration ..	1,500	1,500	6,000
	<hr/>	<hr/>	<hr/>
	5,500	8,500	34,000
Less Losses, etc. ..			26,000
			<hr/>
			8,000
Abatement ..	1,300	700	800
	<hr/>	<hr/>	<hr/>
	£4,200	£7,800	£7,200
	<hr/>	<hr/>	<hr/>
N.D.C. at 5% ..	£210	£390	£360
	<hr/>	<hr/>	<hr/>

A claim would, therefore, be made in cases (a) and (c) but not in case (b).

#### § 14.—Relief for Losses (4th Sch., R. 2—1937).

Provision is made for losses incurred in the trade or business being carried forward and deducted from subsequent profits. The relief applies not only to losses incurred in accounting periods which fall within the N.D.C./P.T. years, but also to losses of pre-N.D.C. years which are available to be carried forward under § 33, 1926, or § 19, 1932, for Income Tax purposes. These must be dealt with on slightly different lines, however.

The addition of the “war years” to the six years for which pre-N.D.C. losses may be carried forward applies to N.D.C. as well as to Income Tax (§ 37—(No. 2) 1945).

There is no time limit for losses incurred in a N.D.C./P.T. accounting period.

For this purpose, the following definitions must be noted :—

“Relevant accounting period.” Any accounting period falling wholly after the 6th April, 1937.

“Year of assessment corresponding to an accounting period.” The year of assessment following that in which that accounting period ends.

In the case of businesses which have to include their investment income in arriving at profits, such income must be included in arriving at pre-N.D.C. losses for the purposes of relief (§ 36—1939).

**(a) Pre-N.D.C. Losses.**

Where a person carrying on a business, either solely or in partnership, has sustained a loss therein before the beginning of the first relevant accounting period, he may claim relief for so much of that loss as could, under § 33, 1926 (as amended by § 19, 1932 and § 37—(No. 2) 1945), be carried forward against the assessment for the Income Tax year of assessment corresponding to that accounting period.

The purpose of the provision is to pick up the loss which is being carried forward for Income Tax purposes and apply it to N.D.C./P.T. As N.D.C./P.T. is assessed on an “actual” basis, whereas Income Tax is assessed on a “preceding year” basis, it has been necessary to provide that the N.D.C./P.T. accounting period is to be deemed to correspond with the following year of assessment, so that the same basic accounts are involved in both taxes. For example, if the accounts of the business are made up to 31st December, annually, those for the year ended 31st December, 1938, give the basis of the N.D.C. assessment for that year, but of the Income Tax assessment for 1939-40. Both assessments are thus based on the same accounts, and 1939-40 is termed the “year of assessment corresponding to the accounting period” for the year to 31st December, 1938, which is a “relevant accounting period,” since it falls wholly after 6th April, 1937.

It should particularly be noted that the commencing date, for this purpose, is 6th April, 1937, and not 1st April, 1937. The reason for this is apparent when it is remembered that the losses in point are for years of assessment, and it is therefore necessary to have regard to the full year, and not a year of assessment less five days.

The underlying principle can be seen more readily from a comprehensive example, employing figures.

#### Illustration.

A company made the following profits and losses as adjusted for Income Tax purposes :—

Year ended November 30th.

1932	.	..	Loss	£18,000
1933	..	..	Profit	1,000
1934	..	..	Loss	3,000
1935	..	..	Profit	2,000
1936	..	..	Profit	4,000

The Income Tax assessments would, therefore, be as follows :—

Year of Assessment.	Assessment based on previous year's accounts.	Deduct Loss brought forward	Balance of Loss carried forward.	Net Assessment
1933-34	nil	—	£18,000	nil
1934-35	£1,000	£1,000	£17,000	nil
1935-36	nil	—	£20,000	nil
1936-37	£2,000	£2,000	£18,000	nil
1937-38	£4,000	£4,000	£14,000	nil

The balance of loss available to be carried forward from 1937-38 is made up of £11,000 from 1932, which cannot be carried forward beyond 1938-39, and £3,000 from 1934 which cannot be carried forward beyond 1947-48, by reason of the six years' time limit in § 33, 1926, as extended by § 37—(No. 2) 1945.

The real effect of carrying forward losses against subsequent assessments is that the loss in 1932 has in substance been set against the profits of the accounting periods ended in 1933, 1935 and 1936.

When we come to the year to 30th November, 1937, we find that it falls partly after 5th April, 1937, and is therefore a "relevant accounting period." Suppose that the adjustments of the profits of that year were as follows :—

	For Income Tax purposes. £	For N.D.C. purposes. £
Net Profit as per Profit and Loss Account .. .. .	10,000	10,000
Add Depreciation .. .. .	300	300
Charitable subscriptions	50	50
Bad Debts (General Reserve) .. .. .	200	200
Debenture Interest .. .. .	1,000	—
Ground Rent of Factory	40	—
	<u>11,590</u>	<u>10,550</u>
Deduct Net Annual Value of Factory .. .. .	80	
Depreciation allowance of Factory .. .. .	20	20
Investment Income .. .. .	400	400
	<u>500</u>	<u>420</u>
	<u>£11,090</u>	<u>£10,130</u>

The adjusted profits for Income Tax purposes form the basis of assessment for Income Tax 1938-39, but those for N.D.C. purposes form the basis of assessment for the chargeable accounting period to 30th November, 1937. The Acts therefore treat these assessments as corresponding to each other, and the loss which can be set against the 1938-39 Income Tax assessment can likewise be set for N.D.C. purposes against the accounts for the relevant accounting period, *i.e.*, the year to 30th November, 1937. Bearing in mind the real effect of the carry forward of losses, it will be seen that the loss is being set against the profits of the same accounting period for both purposes.

The assessments are therefore—

	Income Tax 1938-39. £	N.D.C. April 1, 1937 to Nov. 30, 1937. £
Adjusted profits of year to 30th November, 1937 .. .. .	11,090	10,130
Less Loss brought forward .. .. .	14,000	14,000
Leaving balance of Loss of .. .. .	<u>£2,910</u>	<u>£3,870</u>
Assessment .. .. .	nil (8 months)	nil
The amount of Loss which can be carried forward, owing to the extension of the six years' time limit, is .. .. .	<u>£2,910</u>	<u>£3,000</u>

It must particularly be noted that the loss is set off in the accounting period, not in the chargeable accounting period.

In the above illustration, Wear and Tear has been ignored, but it will be noted that where Wear and Tear allowances have ousted losses, § 19, 1932, gives relief by allowing the losses to be carried forward beyond the six years (as extended where relevant), and such pre-N.D.C. losses can likewise go forward for N.D.C./P.T. purposes.

In the above illustration, the balance of loss for Income Tax purposes is carried forward to 1939-40. Since it is available for relief in that year of assessment, the loss is also available for N.D.C. purposes in the year to 30th November, 1938, the relevant accounting period to which 1939-40 corresponds. It should be noted, however, that the amount of loss to be carried forward for N.D.C. purposes is the balance remaining at 30th November, 1937, for N.D.C. and not the same figure as the Income Tax loss balance.

In other words, the pre-N.D.C. losses available are those which were being carried forward for Income Tax purposes, but the allowable losses are set against the profits as computed for N.D.C./P.T. and not as computed for Income Tax. This follows from the proviso, which reads :—

Provided that, in ascertaining the amount (if any) that could be so carried forward and deducted from or set off against assessable Income Tax profits for a year of assessment corresponding to an accounting period—

- (a) the amount of the assessable Income Tax profits for that year shall be taken to be equal to the amount of the profits arising in that accounting period (computed in like manner as profits arising in a chargeable accounting period are computed for the purpose of the National Defence Contribution but before making any deduction for wear and tear . . . .);

first accounting period for N.D.C. was also the first relevant accounting period. If, however, the first accounting period for N.D.C. happened to end prior to 6th April, 1937, it was not a "relevant accounting period," since no part of it fell within the five years beginning on 6th April, 1937. It follows, therefore, that a pre-N.D.C. loss cannot be set against the profits of such an accounting period.

A loss in such a period, however, was incurred "before the beginning of the first of the relevant accounting periods" and was therefore, itself a pre-N.D.C. loss.

#### **Illustration (1).**

A company makes up its accounts annually to 5th April. In the year to 5th April, 1937, it made a loss, adjusted on N.D.C. principles, of £20,000. This loss is a pre-N.D.C. loss, being in an accounting period which ends before 6th April, 1937, and can be carried forward as such.

The Acts do not refer to losses which are carried forward under § 19, 1928, *i.e.*, as a result of General Rule 21 assessments. So far as relevant accounting periods are concerned, annual payments are normally allowable deductions in arriving at the profits for N.D.C./P.T. purposes, and further relief is unnecessary. In practice, pre-N.D.C. losses under § 19, 1928, are allowed to be carried forward in the same way as pre-N.D.C. losses under § 33, 1926. There is, however, the necessary proviso that in respect of any General Rule 21 assessment for 1936-37, any portion of the annual payment which is chargeable as an expense in the first accounting period for N.D.C. cannot be carried forward.

#### **Illustration (2).**

A company makes up its accounts annually to 30th June. In 1936-37 it was assessed under General Rule 21 in respect of debenture

interest paid on 30th June, 1936, and 31st December, 1936. Since the December interest is charged in the accounts for the year to 30th June, 1937, only the payment made on 30th June, 1936, can be carried forward as a loss for N.D.C. purposes, although the whole will be available for Income Tax purposes.

*Relief for Losses under Section 34—1918.*

The operation of § 34, 1918, will not affect N.D.C. save in-so-far as it may restrict the loss available for carry forward from pre-N.D.C. years under § 33, 1926.

Where businesses previously treated as separate businesses for N.D.C., have to be treated as one business for P.T., the same sums can be carried forward for losses and wear and tear as might have been carried forward if the businesses were still treated separately. This does not apply to any business that ceased before the end of 1946 (§ 43—1947).

**§ 15.—Insurance Companies.**

As regards life assurance companies, the amount of profit allocated to or reserved for policy holders and annuitants is not chargeable to Income Tax on the companies, and is therefore not to be included in the company's profits for the purposes of N.D.C./P.T.

An important relief was given to insurance companies from 1st April, 1938, up to 31st December, 1946, whereby there was excluded from the profits assessable to N.D.C. the amount of investment income (from business other than life assurance or capital redemption business) which exceeded one-and-a-half times the proportion of the investment income which would otherwise have to be included in profits, that the net premium income bore to the value of the investments (*i.e.*, the average value of all the investments and other property of the company, excluding investments and



property held in connection with life or capital redemption business). This does not apply to P.T. (§ 45—1938, § 32—1947).

Pre-N.D.C. losses of an insurance company are computed on the basis of including investment income in the income of the company (§ 36—1939).

If the functions of a subsidiary of an assurance company which carries on life assurance business, consist wholly or mainly in holding investments or other property, and the whole of the ordinary share capital of the subsidiary is held as part of the investments of the life assurance fund, the assurance company may elect that for the purposes of P.T. (including § 16, F.A., 1943, relief on profits set aside for policy holders), the income from such investments or property shall be deemed to be profits of the life assurance business. If only part of the subsidiary's ordinary share capital is so held, a proportionate part of the income is taken (Para. 5, Pt. III, 8th Schedule—1947).

### § 16.—**Building Societies.**

Building societies are not to pay more P.T. (including distribution charge) than 3 per cent. on their profits before charging any interest or dividends paid to members or depositors (§ 42—1947). For N.D.C. the limit was  $1\frac{1}{2}$  per cent. (§ 23—1937). It should be noted that this is a limitation, and if the N.D.C./P.T. chargeable on the ordinary basis of liability is less, the smaller amount is payable. In no case is interest payable to members deductible in adjusting the profits (§ 23—1937).

Where the P.T. payable is so reduced, any distribution charges for subsequent C.A.P's. must be computed as if a reduction had been made and the full amount of tax had been paid.

**§ 17.—Nationalised Undertakings (§ 40—1947).**

Where the Crown are the only persons beneficially interested in a company with a share capital, P.T. is to be paid as if no distributions had been made, *i.e.*, they pay only 10%.

There are also provisions that certain nationalised undertakings shall not be exempted as statutory undertakings, and that certain payments of interest shall not be deductible in computing profits of specified concerns. These are not of general interest.

**§ 18.—Industrial and Provident Societies (§ 41—1947).**

Co-operative and similar societies are given the benefit of being taxed as if they had made no net relevant distributions, *i.e.*, they pay only 10%.

**§ 19.—Groups of Companies (§ 22—1937 ; § 42 and 4th Sch.—1938 ; § 38—1947).**

In the following explanation, the terms “ company ” and “ subsidiary ” or “ subsidiary company ” are employed for convenience, but it must be borne in mind that the Acts apply to any “ body corporate.”

Provision is made for a holding company and its subsidiaries to be treated as a single unit for the purpose of assessment to N.D.C. on notice being given by the parent company.

Where a company beneficially owns, either directly or through another or other companies, not less than three-quarters of the ordinary share capital (as defined in § 9 of this Chapter) of a subsidiary company, it may give written notice requiring the profits or losses of the subsidiary company to be treated as if they were its own profits or losses. The notice must be given during, or

within six months from the end of the chargeable accounting period of the subsidiary company for which it is first desired to claim. The Commissioners of Inland Revenue may allow a longer period in any case where they think fit. The claim binds the companies to continue to amalgamate their results for so long as the parent company continues to hold at least three-quarters of the ordinary share capital of the subsidiary. (In respect of periods ended before 29th July, 1938, the time limit was 28th January, 1939.) A notice given before 31st July, 1947, can, however, be revoked by notice before 1st February, 1948, or such extended time as the C.I.R. allow, with effect from 1st January, 1947 (§ 38—1947). Where accounts bridge 31st December, 1946, in such a case, the part to that date and the part after will be separate C.A.P.'s.

Current losses of one company in the group will, if the claim is made, be set against current profits of the other companies. Losses brought forward from previous years into an accounting period can only be deducted from profits of the company that incurred the loss, not from the combined profits.

Similarly, pre-N.D.C. Wear and Tear brought forward can only be deducted from the profits of the company concerned, any excess not being chargeable against another company.

It is also provided that if a loss has already been the subject of relief by having been set off against the profits of another company, it cannot also be carried forward (§ 43—1938).

Describing the provisions, the Financial Secretary in Parliament said—

“The object is to meet the case of the business which is essentially one business in a single ownership, although in form it is carried on through the medium of one or more companies, namely,

a parent company, which is generally responsible for the finance and management of the whole concern, and one or more subsidiary companies which carry on the actual trade . . . . .

“The profits of each company are, of course, separately assessable to Income Tax as an independent trade or business, and, if there were no provision of this kind, those profits would be separately assessable to the National Defence Contribution, and each company would separately benefit by the exemption in cases in which the profits fall below £2,000, and by the scale of abatements up to £12,000. In the case, however, of the type of companies to which this Clause will mainly apply, where there is a holding company which carries on what is really one trade or business through the medium of one or more subsidiary companies, it seems reasonable that the business should be looked at as a whole, and its liability computed as if it were in fact a single business. This will enable losses in one branch of the business to be deducted from the profits made in other branches. On the other hand, there is an option, because, if the profits of a company are merged in the profits of its parent company, it will of course lose the benefit with regard to exemptions or abatement to which it would be entitled if it were separately assessed.

“Let me give an example of the type of case which seems to us to make some provision of this kind necessary. A parent company may hold all the ordinary shares in a subsidiary company, which is the concern that actually does the trading and makes the profits. The subsidiary company is assessable to National Defence Contribution on its total profits, and those profits, on reaching the parent company in the form of dividends, are, of course, exempt from further taxation. If the parent company uses part of those dividends in paying interest on its debentures—a charge which it must meet—and if it has no other profits assessable to National Defence Contribution from which it could deduct the amount of the debenture interest and the option conferred by the Clause is exercised, it will be able to deduct from the profits of its subsidiary company the interest paid on the debentures. This is restricted to cases where both bodies are resident in the United Kingdom. The House will know, of course, that a company is resident in this country for purposes of Income Tax, and of National Defence Contribution, if it is controlled in the United Kingdom. The Clause is not intended to apply to a foreign company which is assessed to National Defence Contribution only for business carried on in this country.

“Another point is this : If the option is exercised, the provisions for the amalgamation of profits are to apply throughout the duration of the Act as from the first chargeable accounting period in respect of which the notice is given. It is considered that the principal company, having made up its mind to take advantage of this provision to secure a set-off, should not thenceforward be allowed to

chop and change about so as to obtain, during periods when profits are being made, the advantage of separate assessment coupled with the benefit of the exemption or abatement provisions. The notice, of course, ceases to have effect if the subsidiary ceases to be a subsidiary . . . . On Income Tax principles [losses or wear and tear brought forward] would be deductible only from the profits of the company that suffered the losses and it would be inappropriate if, as the result of the amalgamation of profits which we are proposing to grant between parent and subsidiary [losses or wear and tear brought forward which exceed the current profits of the subsidiary], should be deducted from the profits of another company. Deductions will continue to be granted so far as possible against the profits of the company which is entitled to deduction, but a deduction against the profits of another company is precluded . . . . If any other course were taken, there would be serious danger of evasion. A principal company, making large profits, could buy up the shares of another company which has made heavy losses in the past and so secure a set-off of those losses. That is a danger that we must guard against . . . . If companies have the option either to take advantage of the provisions of the clause or to remain on separate assessment and get the advantage of the abatements that are available in that case, we believe that there can be no real hardship to those companies which, as holding concerns, control and have [three-quarters] of the shares of the subsidiary companies which make the profits."

Provision is made for determining the interest of a parent company in sub-subsidiary companies, as follows :—

*Provisions for Determining Amount of Capital held through other bodies Corporate.*

1. Where, in the case of a number of bodies corporate, the first directly owns ordinary share capital of the second, and the second directly owns ordinary share capital of the third, the first is deemed to own ordinary share capital of the third through the second, and, if the third directly owns ordinary share capital of a fourth, the first is deemed to own ordinary share capital of the fourth through the second and third, and the second is deemed to own ordinary share capital of the fourth through the third, and so on.

2.—(a) Any number of bodies corporate of which the first directly owns ordinary share capital of a second and the second directly owns ordinary share capital of a third and so on, if they are more than three, are referred to as "a series," likewise any three or more of them are referred to as "a series."

(b) In any series—

- (i) that body corporate which owns ordinary share capital of another through the remainder is referred to as “the first owner”;
- (ii) that other body corporate the ordinary share capital of which is so owned is referred to as “the last owned body corporate”;
- (iii) the remainder, if one only, is referred to as an “intermediary” and, if more than one, referred to as “a chain of intermediaries”;

(c) A body corporate in a series which directly owns ordinary share capital of another body corporate in the series is referred to as an “owner”;

(d) Any two bodies corporate in a series of which one owns ordinary share capital of the other directly, and not through one or more of the other bodies corporate in the series, are referred to as being directly related to one another.

3. Where every owner in a series owns the whole of the ordinary share capital of the body corporate to which it is directly related, the first owner is deemed to own through the intermediary or chain of intermediaries the whole of the ordinary share capital of the last owned body corporate.

4. Where one of the owners in a series owns a fraction of the ordinary share capital of the body corporate to which it is directly related, and every other owner in the series owns the whole of the ordinary share capital of the body corporate to which it is directly related, the first owner is deemed to own that fraction of the ordinary share capital of the last body corporate through the intermediary or chain of intermediaries.

5. Where—

(a) each of two or more of the owners in a series owns a fraction, and every other owner in the series owns the whole, of the ordinary share capital of the body corporate to which it is directly related ; or

(b) every owner in a series owns a fraction of the ordinary share capital of the body corporate to which it is directly related ;

the first owner is deemed to own through the intermediary or chain of intermediaries such fraction of the ordinary share capital of the last owned body corporate as results from the multiplication of those fractions.

6. Where the first owner in any series owns a fraction of the ordinary share capital of the last owned body corporate in that series through the intermediary or chain of intermediaries in that

series, and also owns another fraction or other fractions of the ordinary share capital of the last owned body corporate, either—

- (a) directly ; or
- (b) through an intermediary or intermediaries which is not a member or are not members of that series ; or
- (c) through a chain or chains of intermediaries of which one or some or all are not members of that series ; or
- (d) in a case where the series consists of more than three bodies corporate, through an intermediary or intermediaries which is a member or are members of the series, or through a chain or chains of intermediaries consisting of some but not all of the bodies corporate of which the chain of intermediaries in the series consists ;

then, for the purpose of ascertaining the amount of the ordinary share capital of the last owned body corporate owned by the first owner, all those fractions are aggregated and the first owner is deemed to own the sum of those fractions.

### *Provisions as respects Notices.*

1. No principal company, being itself a subsidiary of another principal company, may give a notice as respects a subsidiary of itself, if and so long as a notice previously given as respects that principal company by that other principal company is in force.

2. Subject to the provisions of the next following paragraph, no principal company may give a notice as respects a subsidiary—

- (a) if and so long as a notice previously given as respects that subsidiary by another principal company is in force ; or
- (b) if and so long as a notice previously given by that subsidiary as respects a subsidiary of itself is in force.

3. Notwithstanding anything in the preceding paragraph (2), where a notice previously given by a principal company (hereafter referred to as the “first subsidiary”) as respects a subsidiary (hereafter referred to as the “second subsidiary”) is in force, and both the first subsidiary and the second subsidiary are subsidiaries of another principal company (hereafter referred to as the “first principal company”), the first principal company may give a notice as respects both the first subsidiary and the second subsidiary, but not as respects one or the other alone :

Where, however, a notice previously given by the first subsidiary as respects one or more other subsidiaries besides the second subsidiary is in force, the first principal company may not give a notice under this paragraph unless—

- (a) that other subsidiary or all those other subsidiaries are subsidiaries of the first principal company ; and

- (b) the first principal company gives a notice as respects that other subsidiary or all those other subsidiaries as well as the first and second subsidiaries.

4. Where a notice is duly given by the first principal company under the preceding paragraph (3), the notice previously given by the first subsidiary as respects the second subsidiary and any other subsidiary cease to be in force.

5. Where a notice is given simultaneously by two or more bodies corporate, the notice given by such one of them as may be agreed upon between them or, in default of agreement, may be determined by the Commissioners of Inland Revenue, is treated as having been given before the other notice or notices.

### Illustrations.

In this illustration "Ordinary share capital" is abbreviated to "O.S. capital."

(1) Where the holdings are not one hundred per cent., the fractions held must be multiplied to find the proportion held, *e.g.*—

A Co. holds	95%	of the O.S. capital of	B Co.
B Co. „	90%	„ „ „	C Co.
C Co. „	100%	„ „ „	D Co.
D Co. „	85%	„ „ „	E Co.
E Co. „	80%	„ „ „	F Co.

Then A Co. is deemed to own—

95% of 90%	..	=	85.5%	of the O.S. capital of	C Co.
95% of 90% of 100%	=	85.5%	„ „ „		D Co.
95% of 90% of 100% of 85%	=	72.675%	of the O.S. capital of	E Co., and so on.	

And C Co. is deemed to own—

100% of 85%	..	=	85%	of the O.S. capital of	E Co.
100% of 85% of 80%	=	68%	„ „ „		F Co.

(2) Where a company is subsidiary to two or more companies, fractional holdings are to be aggregated, *e.g.*—

Where G Co. owns	90%	of the O.S. capital of	H Co.
G Co. „	70%	„ „ „	J Co.
H Co. „	30%	„ „ „	J Co.

Then G Co. is deemed to own 70% + (through H Co.) 90% of 30% = 97% of the O.S. capital of J Co.

The provisions as to notices are designed to prevent a company from amalgamating the profits of companies in which, directly or indirectly, it holds less than 75% of the O.S. capital, and also for preventing the amalgamation of the same profits more than once.



(3) If A Co. is a subsidiary of B Co., and B Co. has given notice as regards A Co., A Co. cannot give notice as regards its own subsidiaries.

(4) If A Co. is a subsidiary of B Co. and of C Co., and B Co. has given notice as regards A Co., C Co. cannot give notice as regards A Co.

If D Co. is a subsidiary of E Co., and F Co. is a subsidiary of D Co., and D Co. has given notice as regards F Co., E Co. cannot give notice as regards D Co.

If, however, G Co. is a subsidiary of H Co., H Co. of J Co., and J Co. of K Co., and H Co. has given notice as regards G Co., J Co. may give notice as regards both H Co. and G Co., or K Co. may give notice as regards J Co., or as regards all the subsidiary companies of each. But if K Co. does not own at least 75% of the O.S. capital of G Co., G Co. is not a subsidiary of K Co., and if an intermediary J or H has given notice as regards G, K cannot give notice as regards J or H (as the case may be).

#### *Investment Income of Holding Companies.*

For the purposes of N.D.C., the profits of any body corporate must include all dividends or other distributions of profits received from any other body corporate in which it has a controlling interest and which is not liable to be assessed to N.D.C. It is to be noted that controlling interest is not defined for this purpose, and is a question of fact (4th Sch., R. 7—1937).

For P.T., if a parent company has elected to include a subsidiary company's profits and losses with its own, then—

- (a) the franked investment income and gross relevant distributions of the subsidiary must be included in the franked investment income and gross relevant distributions respectively of the parent company; but
- (b) no franked investment income received directly by the parent from that subsidiary, or received

directly by the subsidiary from the parent, or directly by the subsidiary from any other subsidiary which is being combined, and no distributions between such companies, are to be so included.

If (i) the net relevant distributions for any C.A.P. in the case of the principle company, exceed the profits chargeable to P.T. and (ii) in any C.A.P. of the subsidiary before the notice to amalgamate the profits and losses came into force, the net relevant distributions of that subsidiary were less than the profits of that C.A.P., so that non-distribution relief was given to the subsidiary on the difference, then the parent company will get relief against the excess in (i) in respect of (ii) to the extent that it has not been otherwise given (*e.g.*, to a previous parent company or to the subsidiary in another C.A.P.).

Where a subsidiary company reimburses its parent P.T. for a C.A.P. ending after 1946, the two companies may elect (within 6 months after the end of the C.A.P. or extended time if the C.I.R. allow) that the amount so paid and any amount so paid for any subsequent C.A.P. shall be allowed as an expense of the subsidiary for Income Tax purposes, and treated as a reduction of the P.T. paid by the parent.

For P.T., the C.I.R. may direct that there shall be alterations in what would otherwise be C.A.P.'s. (§ 38—1947).

The profits of a body corporate which either alone or in conjunction with any statutory undertaking has a controlling interest in another body corporate which is a statutory undertaker, are not to include any income received from the subsidiary body (4th Sch., R. 7—1937; § 32 (1)—1947).

*Inter-company Payments between Associated Companies*  
(§ 42—1938).

Where a body corporate is a subsidiary of another, or two bodies corporate are both subsidiaries of a third, any interest, annuity or other annual payment, or any royalty or rent paid by one to the other is disallowed as an expense of the payer and excluded from the profits of the recipient. This applies only, however, where the paying company is resident or carrying on a trade or business in the United Kingdom. The residence, etc., of the recipient is immaterial.

**§ 20.—Excess Profits Tax Deductions and P.T.**

The following provisions co-ordinate E.P.T. and N.D.C. with consequent effect on P.T. (§ 46 and 8th Sch., Pt. II—1947) :—

Where—

- (i) Deferred repairs have been treated as reducing the profits of an accounting period which, or any part of which is a C.A.P. for E.P.T. purposes (under § 37 (1) (a), 1940) ; or
- (ii) An expense has been “ spread ” for E.P.T. to any such accounting period under § 33 (2) F.A., 1940 ; or
- (iii) A deduction in respect of back-service payments to a superannuation fund would have been allowed were it not for § 23, 1943, or an election has been made under that section for spreading the payments for E.P.T. ; and
- (iv) A deduction in respect of any of the above would have been made in a subsequent accounting period for P.T. purposes or would have been so made but for the fact that the business is carried on by individuals or by individuals in

partnership (so that the profits no longer attract P.T.),

then the same sums shall be deducted in the same periods for N.D.C./P.T. as are deducted for E.P.T. or would have been deducted had E.P.T. continued to be chargeable. In respect of (iii), the taxpayer can elect to spread payments made or incurred before 2nd February, 1943, despite the fact that he had made no election before the passing of the Finance Act, 1947.

Where a sum is spread under § 33 (2), 1940, or § 23, 1943, only such amounts shall be deductible for P.T. after 1946 as would have been deductible for the purposes of E.P.T. had E.P.T. continued to be chargeable.

In the case of rehabilitation or cancellation costs related back to the last C.A.P. for E.P.T., N.D.C. on the profit for the corresponding C.A.P. for N.D.C. is to be reduced by such percentage of these costs as is equal to the rate per cent. at which N.D.C. would have been chargeable on the profits if the F.A., 1947, had not been passed (*i.e.*, 5% or 4% according to the proprietorship) and the costs are not to be allowed as a deduction for P.T. for any accounting period.

#### Illustration.

A company incurred the following terminal expenses:—

In the year ended 31st December, 1947:

(a) Rehabilitation costs, £6,000.

(b) Cancellation costs, £2,000.

In the year ended 31st December, 1948:

(c) Deferred repairs, £12,000.

It had also, in 1946, paid £20,000 to the superannuation fund in respect of back service of employees who had served in the Forces and claimed to spread this back for E.P.T. purposes over the years to which it related.

As the items (a) and (b) above would be allowable for E.P.T. in the C.A.P. ended 31st December, 1946, the N.D.C. for the same C.A.P. would be reduced by the N.D.C. on such costs.

Item (c) would be allowed for E.P.T. in the C.A.P.'s. when the repairs would normally have been executed.

Accordingly, none of the items (a) (b) or (c) would be allowable for P.T. in 1947 or 1948.

The E.P.T. and N.D.C. for the years affected would be recomputed as a result of the spreading of the expense.

If an expense incurred in, say, 1943, was spread forward for E.P.T., the same amounts would be allowed for N.D.C. each year as were allowed for E.P.T. As from 1st January, 1947, the same amounts would be allowed for P.T. as would have remained to be allowed under the "spread" had E.P.T. continued.

## 21.—Assessment and Collection.

N.D.C./P.T. is assessed and collected by the Commissioners of Inland Revenue (*i.e.*, the Board). It is due and payable at the expiration of one month from the date of the assessment. As with Income Tax (*see* Chap. II, § 24), interest is charged at 3 per cent. per annum on arrears exceeding £1,000 (§ 8—(No. 2) 1947). Tax and interest are recoverable as a debt due to His Majesty from the person on whom it is assessed (§ 24—1937). The assessment is made on the person carrying on the trade or business in the chargeable accounting period.

Where two or more persons were carrying on the trade or business jointly in the relevant chargeable accounting period, the assessment is made upon them jointly and, in the case of a partnership, may be made in the partnership name, if any.

Where an assessment could, but for his death, be made on any person either solely or jointly with any other person, the assessment may be made on his personal representative either solely or jointly with that other person, as the case may be.

If a person liable to assessment is not resident in the United Kingdom, an assessment may be made upon any agent, manager, or factor resident in the

United Kingdom through whom the trade or business was carried on in the chargeable accounting period.

An assessment (including an additional assessment) may be made at any time in respect of any chargeable accounting period in respect of which the assessment is made, and in the absence of a satisfactory return or other information on which to make an assessment, the Commissioners of Inland Revenue may make an assessment according to the best of their judgment (5th Sch., Pt. I—1937 ; § 35—(No. 2) 1945).

The error or mistake provisions apply (§ 35—and 5th Sch.—(No. 2) 1945).

The following penalty, etc., provisions apply :—  
§§ 107, 140 ; § 23, 1923 and § 34, 1942 (§ 28 and 8th Sch.—1943).

## § 22.—Appeals.

Any person who is dissatisfied with an assessment to N.D.C./P.T. may appeal either to the General Commissioners for the division in which he is assessed for the purposes of Income Tax, or to the Special Commissioners. The Appeal Commissioners have power, if they think fit, to summon witnesses and examine them on oath.

The appeal must be made in writing to the Inspector of Taxes within 30 days of the date of service of the notice of assessment, or within such further time as the Commissioners of Inland Revenue may allow. The notice of appeal must specify the grounds of appeal and whether the appellant desires the appeal to be heard by the General Commissioners or the Special Commissioners. The Appeal Commissioners may allow other grounds to be gone into if satisfied that their omission from the notice of appeal was not wilful or unreasonable (S.R. & O. No 731, 5th August, 1937).

(There are no General Commissioners in Northern Ireland ; their powers are in the hands of the Special Commissioners. Appeal is allowed from their decision to the recorder or county court judge.)

There is the usual right of appeal to the High Court on a question of law.

Notwithstanding that an appeal is pending, such part of the tax assessed as appears to the Commissioners of Inland Revenue not to be in dispute is to be collected and paid. On the determination of the appeal, any balance chargeable in accordance with the determination becomes payable, or any amount overpaid will be repaid, as the case may require (5th Sch., Pt. II—1937).

Any barrister or solicitor or member of an incorporated society of accountants may be heard on the appeal (S.R. & O. No. 731—1937).

### § 23.—Supplementary Provisions—Returns, etc.

The Inspector of Taxes may by notice in writing require any person who carries on or has carried on any trade or business to which the tax applies to deliver to him a return (in the form prescribed by the Commissioners of Inland Revenue) of the profits arising from the trade or business in any period during which it was carried on by that person and to furnish him with any other particulars relating to the trade or business. If the person in question is dead, or is a body corporate which is being wound up, the notice may be given to the personal representative of the dead person or liquidator of the body corporate, as the case may be. Where the trade or business is or was being carried on by persons in partnership, the notice may be given in the partnership name, if

any. If the person who carries on or has carried on the trade or business is not resident in the United Kingdom, the notice may be given to any agent, manager or factor resident in the United Kingdom through whom he is or was carrying on the trade or business.

Every person to whom a notice is so given must comply with its requirements within one month from the date of the notice. Where a notice is given in the partnership name to the persons who are or were carrying on a trade or business in partnership, it is the duty of the precedent partner or, where no partner is resident in the United Kingdom, of the agent, manager or factor of the firm resident in the United Kingdom, to comply with the requirements of the notice.

Where a body corporate is being wound up, the liquidator of the body corporate must not distribute any of the assets of the body corporate to the members thereof unless he has made provision for the payment in full of any tax which may be found payable by the body corporate.

If any person without reasonable excuse contravenes or fails to comply with these supplementary provisions he is liable on summary conviction to a fine not exceeding five hundred pounds, and if he fails to comply with the requirements, to a further fine not exceeding fifty pounds for every day on which the failure continues.

In a bankruptcy, in the winding-up of a company, and in the event of a receiver being appointed on behalf of the holders of any debentures of a company secured by a floating charge or of possession of any property comprised in or subject to a floating charge



being taken by or on behalf of the holders of any debentures of a company secured by that charge, the same priority is given to N.D.C./P.T. as is, by the enactments relating to bankruptcy and companies, required to be given to Income Tax (5th Sch., Pt. III—1937).

### § 24.—Application of Income Tax Rules to N.D.C.

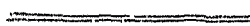
Under powers given to them by the Finance Act, 1937 (5th Sch.), the Commissioners of Inland Revenue made regulations under which the following Income Tax Rules are made applicable to N.D.C./P.T.:—

#### *General Rule.*

#### *Subject Matter.*

- |                                  |  |
|----------------------------------|--|
| 4. 13 and 14 ..                  | The assessment of persons having the direction, control, etc., of the property, etc., of incapacitated persons.                                |
| 8 and 9 ..                       | The assessment of non-resident persons on a percentage of turnover.  |
| 10 (as amended<br>by § 17, 1925) | A non-resident person cannot be charged in the name of a broker or general commission agent, etc.  |
| 11 .. ..                         | The fact that a non-resident person has transactions with another non-resident person does not of itself make him liable on profits therefrom. |
| 12 .. ..                         | The assessment of non-residents through an agent on merchanting profit only.   |

*Note.*—The “error or mistake” provisions (§ 24—1923) now apply to N.D.C./P.T. (§ 37—(No. 2) 1945).



## APPENDIX I.

## RECENT RATES OF INCOME TAX, SUPER-TAX AND SUR-TAX.

Year ..	1925-26 1926-27 1927-28	1928-29 1929-30	1930-31	1931-32 1932-33 1933-34	1934-35	1935-36 1936-37 1937-38	1938-39	1939-40	1940-41	1941-42 to 1945-46	1946-47
Standard Rate .. .. .	4/- 2/-	4/- 2/-	4/6 2/-	5/- 2/6	4/6 2/3	4/6 1/6	5/- 1/8	7/- 2/4	8/6 5/6	10/- 6/6	9/- 75 at 6/-
Reduced Rate .. .. .	2/5	2/5	2/5	2/5	2/5	2/5	2/5	2/5	2/5	2/5	2/5
Amount of taxable income chargeable at Reduced Rate .. .. .	£225	£225	£250	£175	£175	£135	£135	£135	£165	£165	£165
Earned Income Allowance .. .. .	1th	1th	1th	1th	1th	1th	1th	1th	1th	1th	1th
Maximum .. .. .	£250	£250	£250	£300	£300	£300	£300	£300	£250	£150	£150
Old Age Allowance on incomes not exceeding £500 (marginal relief) Taxpayer or Wife over 65 at beginning of year .. .. .	1th	1th	1th	1th	1th	1th	1th	1th	1th	1th	1th
Personal Allowance: .. .. .	£135	£135	£135	£100	£100	£100	£100	£100	£100	£80	£110
Single .. .. .	£225	£225	£225	£150	£170	£180	£180	£170	£170	£140	£180
Married man .. .. .	£225	£225	£225	£150	£170	£180	£180	£170	£170	£140	£180
Additional Personal Allowance: .. .. .	£1th	£1th	£1th	£1th	£1th	£1th	£1th	£1th	£1th	£1th	£1th
Fraction of Wife's Earned Income .. .. .	£1th	£1th	£1th	£1th	£1th	£1th	£1th	£1th	£1th	£1th	£1th
Maximum .. .. .	£45	£45	£45	£45	£45	£45	£45	£45	£45	£45	£45
Child Allowance: .. .. .	£36	£60	£60	£50	£50	£50	£50	£50	£50	£50	£50
One Child .. .. .	£36	£60	£60	£50	£50	£50	£50	£50	£50	£50	£50
Each Other Child .. .. .	£36	£60	£60	£50	£50	£50	£50	£50	£50	£50	£50
Maximum income which Child may have .. .. .	£40	£60	£60	£50	£50	£50	£50	£50	£50	£50	£50
Housekeeper's Allowance .. .. .	£60	£60	£60	£50	£50	£50	£50	£50	£50	£50	£50
Dependant Relative Allowance for widowed mother, incapacitated relative, or daughter on whose maintenance is made owing to own incapacity .. .. .	£25	£25	£25	£25	£25	£25	£25	£25	£25	£25	£25
Exemption to income not exceeding (Marginal relief) .. .. .	none	none	none	none	none	none	none	none	none	none	none

N.B.—In the above table, the rates, etc., remain unchanged where no entry is made under a year of assessment.

\* Children undergoing training added for 1938-39 onwards.

\*\* Extended for 1943-44 onwards as explained in text.

† Claim in respect of relatives denied unemployment allowance, etc., added for 1938-39 onwards.

‡ Claim maximum 1943-44 to 1946-47, £50 (reduced if relative's income exceeds £30), except for daughter (see text).

§ Claim maximum 1947-48, £50, reduced if relative's income exceeds £70 (see text).



## APPENDIX II.

## INCOME TAX—WEAR AND TEAR ALLOWANCES.

*The following is the Schedule of Agreed Rates of Depreciation for the purpose of computing liability to United Kingdom Income Tax, revised to March, 1947.*

## (a) GENERAL NOTES.

1. The rates in the following Schedule which are subject to the approval of the Commissioners concerned, have been agreed by the Board of Inland Revenue and an association or associations representing the users of the plant and machinery. The application of these rates is not, however, limited to members of any particular association.

2. (a) For years up to 1946-46 inclusive, except in the cases of shipping and tramways all allowances are calculated on a written-down value deemed to be that as at the commencement of the year of assessment.

(b) For 1946-47 and subsequent years, except in the case of shipping and tramways, all allowances are to be calculated on the written-down value of the machinery or plant in use at the end of the basis period for the year of assessment (§ 16 (1)—Income Tax Act, 1945).

3. All additions to, and renewals and replacements of, plant and machinery in respect of which an allowance for wear and tear is made, are treated as a capital outlay, except that renewals and replacements of parts of a machine which do not destroy its identity are allowed as a business expense.

4. Unless specially provided for in the agreement with the particular industry, a claim for an increased rate of allowance on account of the use of the machinery and plant over and above that by reference to which the estimated life has been computed is considered in the light of the particular circumstances of each individual case.

5. The figures in this Schedule take no account—

- (a) of the additional deduction of one-fifth; of the deduction in respect of wear and tear granted by § 18, 1932, as amended by § 22, 1938, for years up to 1945-46 inclusive; or
- (b) of the provision of § 16 (2), Income Tax Act, 1945, by which, for 1946-47 and subsequent years of assessment, the wear and tear deductions are to be increased by one-quarter of the amount considered by the Commissioners to be just and reasonable.

## (b) Rates for Particular Industries.

AIRCRAFT AND AIRCRAFT ENGINE MANUFACTURE	%	APRON MAKING (see CLOTHING—LIGHT).	%
High speed precision plant (i.e., plant designed to work to a degree of accuracy of not less than 1/1,000th of an inch margin and normally engaged on such work), heat treatment, plating and electric welding plant ..	12½	ARTIFICIAL SILK (see SILK).	
Other plant and machinery .. ..	7½	BAKERY	
For years to 1946-47, for plant and machinery working continuously, i.e., treble shift, or double shift plus overtime, the above rates to be increased by 50 per cent. thereof.		Plant and Machinery generally ..	8
For 1947-48 onwards, where working in any case exceeds a complete double shift, a claim to an increased allowance will be dealt with on its merits.		For 1941-42 onwards, an increased allowance, the precise amount of which is to depend on the facts of the individual case, is made to meet war-time conditions, e.g., abnormally long working hours and increased production.	
Accounting machines .. ..	10	The non-metal parts of the structure of ovens are included for wear and tear purposes, as part of the bakery plant and machinery.	
Motor cars and lorries .. ..	20		

BLEACHING AND FINISHING		%	CLAY INDUSTRIES (continued)		%
Plant and machinery generally ..		7½	<i>Heavy clay industry</i> (excluding building brick manufacture but covering manufacture of roofing and flooring tiles, refractory goods, sanitary pipes and fittings, enamelled bricks and tiles, terracotta goods, sanitary fire-clay goods, red clay goods and similar articles) and		
BLOUSEMAKING (see CLOTHING—LIGHT).			<i>Pottery manufacture</i> (manufacture of china ware, earthenware, electrical porcelain, glazed tiles, sanitary ware, sanitary fire-clay and jet Rockingham goods).		
BOLT, NUT, SCREW AND RIVET MANUFACTURE			Steam engines, boilers, shafting and general plant and machinery, e.g., piping, mixing, shaping and glazing machines (blungers, tanks, arks, sifters, pumps, jiggers, jolleys, presses, etc.), conveyers, trucks (or cars), propelling mechanism and tracks, air supply and exhaust fans and dust extraction plant ..		5 *
Plant and machinery generally ..		10	Crushing and grinding plant (milling plant) ..		7½*
Electric furnaces ..		12½	Electrical plant (dynamos, motors, transformers, fans, etc.) ..		7½*
Furnaces (other than electric furnaces), taps and dies, to be dealt with on a renewals basis.			Gas producing plant (Wellman-Galusha type) ..		7½*
(To 1942-43 the above-mentioned rates are to be regarded as covering circumstances of overtime or continuous working.)			Coal pulverising plant and mechanical stokers ..		7½*
For 1943-44 onwards: (a) plant and machinery generally—the rate of 10 per cent. is to be regarded as covering all conditions of working up to, and including, a complete double shift. Where the working in any case exceeds a complete double shift, a claim to an increased allowance will be dealt with on its merits.			Diesel oil engines ..		10*
(b) Electric furnaces—the rate of 12½ per cent. is to be regarded as covering all conditions of working.			Ovens and kilns (see also notes (a) to (f)) ..		10*
BOOKBINDING			* (The above-mentioned rates are to be regarded as covering circumstances of overtime and continuous working.)		
Engines, boilers and shafting ..		5	(a) Hovels constituting a separate structure are not eligible for wear and tear allowance but the cost of rebuilding, or obsolescence, is allowed.		
General binding machinery ..		7½	(b) Greenhouses, tunnel dryers and drying sheds, of a specialised type not forming part of any other structure and constructed and used throughout solely for brick or clay drying purposes, are to be eligible for renewals allowance.		
BRASSFOUNDING			(c) Kilns to include kiln chimneys where an integral part of a kiln (so that the kiln cannot be separately renewed) for the purpose either of a wear and tear or a renewal allowance. No allowance is to be made for wear and tear on, or the complete renewal of, a chimney forming a separate unit.		
Engines, boilers and shafting ..		5	(d) Where wear and tear is allowed, allowances for renewal of parts of a kiln are not to include the cost of complete re-building of the furnace zone of a continuous oven or kiln, but the appropriate obsolescence allowance may be made.		
Electric motors, dynamos and other electrical plant ..		7½	(e) In the case of a continuous oven or kiln, wear and tear and written down value of ancillary machinery, etc., are to be separately calculated by reference to the rate or rates applicable to that machinery.		
Other plant and machinery ..		7			
BRICKMAKING (see CLAY INDUSTRIES).					
CHEMICAL MANUFACTURE					
Chemical plant other than Sulphuric Acid plant ..		7½			
Electrical plant ..		7½			
Other plant ..		5			
(See also SULPHURIC ACID.)					
CHILDREN'S CLOTHING (see CLOTHING—LIGHT).					
CINEMAS					
Projectors ..		15			
Organs ..		7½			
Seating ..		7½			
CLAY INDUSTRIES					
<i>Brick manufacture (building bricks).</i>					
Plant and machinery (excluding kilns), Steam engines, boilers, shafting, and mixing and brick-making machines		5			
Electrical plant (dynamos, motors, transformers, etc.) ..		7½			
Crushing and grinding plant ..		7½			
Kilns (see also notes (b) to (f) below)		10			

CLAY INDUSTRIES (*continued*).

(f) *Change over from renewals to wear and tear basis (at option of taxpayer).* The "starting value" is normally to be the written down value (see the preceding note). Where the original cost of a particular oven or kiln cannot be satisfactorily ascertained, the oven or kiln is to be excluded from the computation and a renewal allowance is to be given on replacement, wear and tear being allowable on the new kiln for the fiscal years following that fiscal year for which the renewal allowance was given.

CLEANING (*see* DYEING AND CLEANING).

CLOTHING—HEAVY (MEN'S)	%
All plant and machinery .. ..	9
Plant and machinery used mainly for work on army clothing contracts as from 6th April, 1939 .. ..	11½

## CLOTHING—LIGHT (LADIES' AND CHILDREN'S)

Engines, boilers and shafting .. ..	5
Electric motors .. ..	7½
General machinery (process plant) .. ..	10

## COKE PRODUCTION

Coke-ovens and ancillary plant .. ..	12½
(Rate to be reconsidered in 1948-49.)	

COLD STORES (*see* ICE).

## COLLIERIES

Railway wagons .. ..	6½
Surface plant and machinery, other than electrical plant .. ..	6½
Electrical plant at the surface and all underground plant installed in the shaft pillar .. ..	7½
Other underground plant .. ..	10
Steam lorries .. ..	15
Lorries driven by internal combustion engines .. ..	20

COLOUR, MANUFACTURE (*see* PAINT).

## CORSET MANUFACTURE

Engines, boilers and shafting .. ..	5
Laundry and cutting machinery .. ..	7½
Electric motors .. ..	7½
Other machinery .. ..	10
Motor vans .. ..	20

## COTTON SPINNERS AND MANUFACTURERS: EXPENDITURE ON ADAPTATION OF PLANT AND MACHINERY

Expenditure upon adaptation of plant and machinery in the Cotton Industry arising out of the introduction of the "more looms per weaver" system can usually be classified under the following headings:—

- (1) New shuttles and shuttle stands
- (2) New pulleys.
- (3) Spare cloth rollers and brackets.

COTTON SPINNERS, ETC. (*continued*)

- (4) Warp stop motions.
- (5) Weft stop motions.
- (6) Shuttle boxes extended.
- (7) Sley repairs and renewals.
- (8) Fitting two box motions.
- (9) Pick and pick motions.
- (10) Conversion of ordinary looms to circular box looms for weaving ordinary cloths.
- (11) Pick counters.
- (12) Alterations to ring spinning frames (new ring rails).
- (13) New ring bobbins.
- (14) Alterations to mule frames to make larger cops.
- (15) High speed drafting (for use in cheaper cottons).
- (16) Rewinding machinery.
- (17) Automatic wet feeding attachments.

It has been agreed that the outlay in question should, subject to the approval of the Commissioners concerned, be dealt with in the following manner:—

(1) *New shuttles, etc.:* and (13) *new ring bobbins*

Outlay under these headings may be dealt with as if it represented expenditure on further supplies of the ordinary type; surplus stocks of the old type may be allowed to lapse from the stock figure.

(7) *Sley repairs and renewals*

In view of the difficulty of distinguishing between outlay under this heading arising in the ordinary way and outlay arising in connection with the adaptation, the whole may be regarded as revenue expenditure.

(16) *Rewinding machinery*

These machines are complete and separate and the normal rate of wear and tear for process plant is to be applied.

*All other headings*

The outlay is to be regarded as capital expenditure, but a special rate of wear and tear allowance, *i.e.*, 12½ per cent. on written-down value, is to be applied for the first five years following the date of the outlay. The balance remaining is then to be treated as process plant, on which the ordinary rate (normally 7½ per cent.) is to be allowed unless some further arrangement is then made.

## CREAMERIES, DAIRIES AND ICE CREAM FACTORIES %

Steam boilers, steam and gas engines and storage tanks .. ..	5
Refrigerating plant (except iceless cabinets) and bottling and washing machines .. ..	10
Iceless cabinets .. ..	15
Other plant and machinery, including electric motors .. ..	7½
(Loose plant, box cycles, utensils (churns, bottles, etc.) and piping are dealt with on renewals basis.)	



ELECTRICITY UNDERTAKINGS (*continued*)

per cent. from the date of completion.

The cost of repairs and maintenance of the shell internal fittings is allowed as a charge against revenue. Where, however, the internal fittings are renewed in their entirety they are regarded as additions; in such a case any appropriate obsolescence or balancing allowance is made.

- (b) Each item (*i.e.*, lamp column, clock controller or set of gear) is treated as a separate unit, the cost of renewal being disallowed as a revenue expense, but admitted as the subject of any appropriate obsolescence or balancing allowance claim.

The cost of connecting the lamp columns with the mains is allowed as a trading expense as and when incurred. All contributions received by the undertaking towards the cost of such services are credited in arriving at the amount of the expenditure to be allowed.

- (c) The term "appliance" includes such wiring leads as require to be renewed upon replacement of the particular appliance which they serve.

- (d) No allowance is made for wear and tear, but annual expenditure on repairs and renewals is allowed as a working expense as and when incurred.

## EMBROIDERY MANUFACTURE

Plant and machinery generally .. 7½

ENGINEERS' PRECISION TOOLS  
MANUFACTURE

To 1945-46 inclusive:

Steam and gas engines, boilers, shafting and pulleys .. 5

Electric machinery, including dynamos and motors .. 7½

Other plant and machinery .. 9

(These rates apply to plant and machinery employed in the manufacture of, *e.g.*, twist drills, milling cutters, reamers, tap dies and screwing tackle.)

1946-47 onwards:

The arrangements relating to Machinery Tool Manufacture is applicable ..

## ENVELOPE MAKING

Steam power plant and shafting .. 5

Electrical power plant, including dynamos and motors .. 7½

All machinery used for the purpose of making envelopes .. 7½

Motor lorries and motor vans .. 20

## FARMING

Steam boilers and engines, portable steam engines, threshing machines and fixed plant .. 5

Electrical installations .. 7½

FARMING (*continued*)

%

Steam lorries .. 15

Binders, reapers and combine-harvesters .. 15\*

Motor lorries and vans driven by internal combustion engines .. 20

Petrol or oil-driven tractor-cultivators 22½

Sprayers and flax pulling machinery 25\*

All other types of farm machinery and implements, including portable poultry (and similar) sheds and incubators .. 10

(No allowance is made in respect of minor loose plant and utensils, but the cost of renewals is allowed as a charge against revenue. Allowance is granted in respect of motor cars used for business purposes at the same rate as for motor lorries, restricted, however, to the proportionate part applicable to such use.)

## FERTILISER MANUFACTURE

Engines, boilers and shafting .. 5

Sulphuric acid plant .. 15

Other plant and machinery .. 10

The rates cover all conditions of working *except* as regards "other plant and machinery" the rate for which is increased to 12½ per cent. where the plant and machinery are worked continuously, *i.e.*, treble shift or double shift plus overtime.

FIBRE, ROPE, NET AND TWINE  
MANUFACTURE

Steam and/or water motive power plant 5

Rope walk machinery and plant .. 5

Electrical machinery and plant .. 7½

Diesel engines .. 10

Process machinery and plant purchased new after 5th April, 1930 .. 10

Other process machinery and plant .. 7½

## FILE AND RASP MANUFACTURE

Electric motors, grinding machines, drop hammers, goff hammers and power stamps .. 7½

File cutting and rasp punching machines .. 6½

All other plant and machinery .. 5

(No allowance is made in respect of grinding and other wheels, utensils, belting, electric cables or furnaces, but the cost of repairs and replacements is allowed as a charge against revenue: the cost of additions to or enlargements of such wheels, utensils, belting, cables or furnaces is treated as capital expenditure in the ordinary course.)

## FISHING TACKLE MANUFACTURE

Engines, boilers and shafting .. 5

Fishing hook and rod making machinery .. 6

Electric motors .. 7½



<b>FLAX SPINNING AND LINEN WEAVING</b> (NORTHERN IRELAND)		%	<b>GAS UNDERTAKINGS</b> ( <i>continued</i> )		
Plant and machinery generally ..	7½		hitherto been dealt with on a renewals basis, elect to claim allowance for expenditure on renewals as and when incurred in lieu of annual wear and tear allowance.		
(No allowance is made in respect of accessory plant such as pins, pin cages, spools, belting, driving ropes, damask cards, designs, patterns, models, furniture and fixtures.)					
<b>FLOCK MANUFACTURE</b>			<b>2. Public Lighting—</b>		%
Motive plant and machinery (steam or water) ..	5		(i) Lamp columns ..	3	
Other plant and machinery ..	7½		(ii) Lamps, clock controllers and gear (In each case on written-down value.)	12½	
(The above-mentioned rates are to be regarded as covering circumstances of overtime or continuous working.)			(Each lamp column, lamp, clock controller and set of gear, will be treated as a separate unit, the cost of renewal being disallowed as a revenue expense, but admitted as the subject of any appropriate obsolescence claim.)		
<b>FLOOR CLOTH MANUFACTURE</b> ( <i>see LINOLEUM</i> ).			<b>GAUGE AND PRECISION TOOL MANUFACTURE</b>		
<b>FLOUR MILLING</b>			To 1945-46 inclusive:		
Steam power plant and shafting ..	5 *		<i>See</i> ENGINEERS' PRECISION TOOL MANUFACTURE		
Electric motors and other electric plant, gas and oil engines, other than Diesel type engines, roller mills, automatic weighers, elevators and conveyors (with legging) and spouting ..	7½ *		1946-47 onwards:		
Other plant and machinery, including Diesel type engines ..	10 *		The arrangement applicable to machine tool manufacture is applicable		
* Rate increased by 20 per cent. for the period 3rd September, 1939, to 6th April, 1947.			<b>HANDKERCHIEF AND EMBROIDERY MANUFACTURE</b>		
<b>FURNITURE MANUFACTURE</b>			Engines, boilers, shafting and gearing and motors ..	5	
Engines, boilers and shafting ..	5		Stitching machines ..	10	
General plant and machinery ..	7½		<b>HEAVY CLAY INDUSTRY</b> ( <i>see</i> CLAY INDUSTRIES).		
Electric motors ..	7½		<b>HEMSTITCHING</b>		
Steam wagons and lorries ..	15		Engines, boilers, shafting and gearing and motors ..	5	
Motor wagons and lorries driven by internal combustion engines ..	20		Hemstitching machines ..	10	
<b>GAS UNDERTAKINGS</b>			<b>HOSIERY MANUFACTURE</b>		
<b>1. Plant and Machinery:</b>			Steam engines, boilers and shafting ..	5	
<b>(i) Manufacture—</b>			Electric motors ..	7½	
Coke-handling plant, pan ash and linker plant, chemical plant, benzol plant, sulphate of ammonia plant, tar distillation plant ..	7½		All process plant ..	13	
Other plant and machinery, excluding concrete cooling towers and masonry tar tanks ..	5		(The rates are to be regarded as covering circumstances of overtime or continuous working.)		
<b>(ii) Distribution (excluding Public Lighting):—</b>			<b>HOSIERY NEEDLE MANUFACTURE</b>		
Gas holders (including tanks and costs of installations), cast iron mains ..	3		Steam and gas engines, boilers and shafting ..	5	
Steel mains ..	5		Electric motors ..	7½	
Meters ..	7½		Process (or manufacturing) machinery	10	
Cookers and fires let out on hire ..	15		<b>ICE CREAM FACTORIES</b> ( <i>see</i> CREAMERIES).		
Other appliances let out on hire ..	20		<b>ICE MANUFACTURE AND COLD STORES</b>		
(In each case on the written-down value.)			Steam and gas engines, boilers and shafting ..	5	
<b>NOTE.—</b> The company may, as regards any of the above-mentioned categories of plant and machinery which have			Electric plant and insulation ..	7½	
			Refrigerating machinery, i.e., compressors, condensers, ice tanks, coolers, conduits, moulds, coils, travellers, etc ..	10	
			(No allowance is made in respect of lagging, belting, loose plant, utensils, etc., but the cost of renewals and replacements is allowed as a charge against revenue.)		

<b>IRON AND STEEL MANUFACTURE</b>		%	<b>LINOLEUM AND FLOOR CLOTH MANUFACTURE</b>		%
Plant and Machinery generally ..	7½		Engines, boilers and shafting ..	5	
Furnace structures (other than electric furnaces) ..	7½		Diesel engines ..	10	
As regards furnace structures a separate option to change from the renewals to the wear and tear basis may be exercised by the taxpayer in relation to any individual range or plant, provided he does so in respect of the whole of the furnaces comprised therein, viz:—			Other plant ..	7½	
(a) A range of blast furnaces, including hot blast stoves and calcining kilns.			<b>LOCOMOTIVE MANUFACTURE</b>		
(b) Steel melting furnaces and mixers included in an individual steel plant.			Boilers, engines, shafting and slow-moving plant and machinery ..	5	
(c) Regenerative and other furnaces and soaking pits attached to an individual rolling mill.			Electric motors, dynamos, and other electric plant; high speed metal working machinery, viz., lathes, drilling, milling, planing, shaping and similar machines ..	7½	
			(No allowance is made in respect of furnaces, but the cost of repairs and replacements and rebuilding is allowed as a charge against revenue; the cost of additional furnaces and extension to existing furnaces is treated as capital expenditure in the ordinary course.)		
<b>JUTE SPINNING AND WEAVING</b>			<b>MACHINE TOOL MANUFACTURE</b>		
Engines, boilers and shafting ..	5		Steam engines, boilers and shafting ..	5	
First and second drawing frames, roving frames, spinning frames, and dressing machines ..	10		Other plant and machinery, including electrical:—		
Breakers and finishers acquired after 6th April, 1937 ..	10		1941-42 to 1944-45:		
Other plant and machinery ..	7½		For all conditions of working, short of a complete double shift ..	7½	
(The rates are to be regarded as covering circumstances of overtime or continuous working.)			For double shift working:		
			Precision plant and machinery (i.e., plant designed to work to a degree of accuracy of not less than 1/1,000th of an inch margin, and normally employed on such work)	12½	
			Remainder ..	7½	
			For continuous working, i.e., treble shift or double shift plus overtime:		
			Precision Plant and Machinery ..	18½	
			Remainder ..	11½	
			1945-46 onwards:		
			For all conditions of working up to, and including, a complete double shift:		
			Precision Plant and Machinery ..	12½	
			Remainder ..	7½	
			1946-47 onwards:		
			Accounting machines and other similar office appliances ..	10	
			1945-46 to 1946-47 only:		
			For continuous working, i.e., treble shift or double shift plus overtime:		
			Precision Plant and Machinery ..	18½	
			Remainder ..	11½	
			For 1947-48 onwards, where working in any case exceeds a double shift a claim to an increased allowance will be dealt with on its merits.		
			The agreement does not apply to plant and machinery used in the manufacture of grinding and other similar machinery. No allowance is made in respect of furnaces, but in lieu thereof the cost of repairs and replacements and rebuilding is allowed as a charge against revenue; the cost of additional furnaces and of extensions to existing furnaces is treated as capital expenditure in the ordinary course.		
<b>LACE AND EMBROIDERY MANUFACTURE</b>					
Plant and machinery generally ..	7½				
<b>LADIES CLOTHING (see MANTLES).</b>					
<b>LADIES LIGHT CLOTHING MANUFACTURE (see CLOTHING—LIGHT).</b>					
<b>LAUNDRIES</b>					
Plant and Machinery generally ..	7½*				
Motor Vans ..	20				
* For 1944-45 to 1946-47 inclusive this may be increased to 11½ per cent.					
<b>LIGHT METAL CASTINGS MANUFACTURE</b>					
Electric furnaces (to cover all conditions of working) ..	12½				
Other plant and machinery (to cover conditions of working up to and including double shift. Where working exceeds double shift each case will be dealt with on its merits) ..	10				
<b>LIGHT RAILWAYS (see TRAMWAYS AND LIGHT RAILWAYS).</b>					
<b>LINEN WEAVING (see FLAX SPINNING).</b>					

<b>MADRAS MANUFACTURE</b>		%	<b>NAIL MANUFACTURE</b>		%
Plant and machinery generally	..	7½	Plant and machinery generally	..	5
<b>MANTLES AND LADIES' CLOTHING</b>			<b>NEEDLE MANUFACTURE</b>		
Engines, boilers and shafting	..	5	Engines, boilers and shafting	..	5
Electric motors	..	7½	Needlemaking machinery and electric motors	..	7½
General machinery (process plant)	..	10	(See also HOSIERY NEEDLE MANUFACTURE.)		
<b>MATCH MANUFACTURE</b>			<b>NEWSPAPER PRINTING</b>		
Steam engines, boilers and shafting	..	5	Engines, boilers and shafting	..	5
Lathes, wood-cutting and wax taper-making machinery, including taper drums	..	5	Printing machines	..	7½
General plant and machinery, including electric dynamos and motors, match-making, splint levelling and cleaning and box filling machines	..	7½	Type	..	10
Motor lorries and motor vans	..	20	(Normally no allowance is given in respect of type, but the actual cost of renewals is allowed as a charge against revenue.)		
(For the purpose of General Note 3 above, a complete "match chain" is to be treated as a complete machine and not as a part of a machine.)			(Where the same machines are used to print morning and evening papers, applications for increased allowance are dealt with on their merits, having regard to proof on the following points.—		
(Where plant and machinery is used by night as well as by day ("double running" or "day and night working") no extra allowance is granted in respect of steam-raising plant, but an extra allowance of 25 per cent. of the normal rates is given in respect of such other plant and machinery as is run both day and night, for the proportional part of the year during which it is so run; no extra allowance is made for any overtime running which falls short of a full day and night.)			(a) life of plant substantially reduced;		
			(b) additional wear and tear not made good by extra expenditure on maintenance and renewal of parts;		
			(c) actual hours of running exceptional (e.g., machines which print only one paper may normally run longer hours than those which print two papers.)		
<b>MILK BARS</b>			<b>NITRIC ACID MANUFACTURE</b> (see DYE-STUFFS).		
Milk and ice cream refrigerating and delivery units	..	15	<b>OVERALL MANUFACTURE</b> (see CLOTHING—LIGHT).		
Carbonating plant, sterilising and washing plant and boilers	..	10	<b>PAINT, COLOUR AND VARNISH MANUFACTURE</b>		
Other plant and machinery	..	5	Engines, boilers, shafting and storage tanks	..	5
<b>MOTOR LORRIES, PANTHECTIONS AND VANS, COMMERCIAL</b> (see end).			General plant and machinery, including grinding machinery and electric motors	..	7½
<b>MOTOR OMNIBUSES</b> (see end).			Motor lorries and motor tractors	..	20
<b>MOTOR VEHICLES WITH INTERNAL COMBUSTION ENGINES, MANUFACTURE OF</b>			(No allowance is made in respect of horses, loose tools or utensils, including typewriters. The arrangement does not apply to ore crushing machinery.)		
Steam engines, boilers and shafting	..	5	<b>PAPER BAG MANUFACTURE</b>		
High Speed precision plant	..	12½*	Engines, boilers and shafting	..	5
Other manufacturing plant and machinery, and electric motors	..	7½*	General plant and machinery, and electric motors	..	7½
Accounting, calculating and other similar office appliances	..	10	Motor vans	..	20
(For 1939-40 to 1946-47 inclusive the allowances in the 12½ and 7½ per cent. categories are increased by 50 per cent. where such plant and machinery is worked continuously, i.e., on trouble shift or double shift, plus overtime.)			<b>PAPER BOX MANUFACTURE</b>		
For 1947-48 onwards, where working in any case exceeds a complete double shift, a claim to an increased allowance will be dealt with on its merits.			Plant and machinery generally	..	7½
			Motor vans	..	20

## PAPER MILLS

Machinery working by day only ..	5
Machinery working day and night ..	7½
(Paper-making is a continuous process. A number of machines, each dealing with a stage of manufacture, are linked up to form one productive unit. For the purpose of General Note 3 above, each machine is treated as a separate item of plant and not as a part.)	

PIG IRON AND STEEL MANUFACTURE  
(see IRON AND STEEL).

## PLASTIC MOULDING

Plant and machinery generally	
The rates depend on the weekly hours worked, viz.—	
Less than 9½ hours ..	10½
9½ hours to 125 hours ..	13
exceeding 125 hours ..	15
The arrangement is applicable to plant used in the plastics industry in the manufacture of laminated materials.	

## POTTERY MANUFACTURE (see CLAY INDUSTRIES).

## PRINTING

Engines, boilers and shafting ..	5
Printing and binding machines ..	7½
Type .. .. .	10
(Normally no allowance is given in respect of type but the actual cost of renewals is allowed as a charge against revenue.)	
Special and delicate machinery is dealt with according to the facts of each case.	
(See also NEWSPAPER PRINTING.)	

## RAILWAY WAGONS OWNED BY PRIVATE TRADERS (see end) .. 6½

READY MADE TAILORING (MEN'S)  
(see CLOTHING—HEAVY).

## RIVET MANUFACTURE (see BOLT, NUT, SCREW AND RIVET MANUFACTURE).

## ROAD ROLLERS (see end).

## SAW MILLING (see TIMBER MERCHANTS).

## SHIPPING

For the period 3rd September, 1939, to 5th April, 1947, the normal allowance for wear and tear of ships is increased by one-quarter. The increased allowance is subject to the additions mentioned in paragraph 5 of the General Notes.

## SHIPPING (continued)

1. In the case of a new ship, the allowance (other than that for refrigerating plant and insulation) is computed on the following basis:—

- (a) sailing vessels .. 3 per cent. on prime cost.
- (b) steamers and motor vessels—  
(i) delivered before 1917 or after 1922 and before 1940 .. 4 per cent. on prime cost.

- (ii) delivered during the period 1917-1922 and 1940-46 .. one twenty-fourth of the difference between prime cost and break-up value.

- (c) tankers .. 5 per cent. on prime cost.

"Prime cost" means the cost price of the vessel, exclusive of the portion relating to refrigerating plant and insulation. As to subsequent capital expenditure, see paragraph 3 below.

2. The break-up value of the vessel, exclusive of the refrigerating plant and insulation, is computed on the basis of a percentage of prime cost:—

- (a) sailing vessels .. .. . 3%
- (b) steamers and motor vessels—  
(i) delivered before 1917 or after 1922 and before 1940 .. 4
- (ii) delivered in—  
1917 .. .. . 3  
1918 .. .. . 3  
1919 .. .. . 1½  
1920 .. .. . 1½  
1921 .. .. . 2½  
1922 .. .. . 3
- (iii) delivered in:—  
1940 .. .. . 3  
1941 .. .. . 2½  
1942 .. .. . 2  
1943 .. .. . 2  
1944 .. .. . 2  
1945 .. .. . 2  
1946 .. .. . 1½
- (c) tankers .. .. . 5½

- (d) In the case of ships acquired under the Government disposal scheme the break-up value is taken as 4 per cent. of the cost to the shipowner.

The break-up value, as computed above, remains constant throughout the life of the ship, i.e., it is not affected by the capital expenditure or by the sale of the ship.

3. Any expenditure which has been treated as capital for tax purposes (e.g., renewal of engines and boilers, or structural improvements) is added to the prime cost of the ship for the purpose of computing the aggregate allowance to be made.

## SHIPPING (continued)

As regards sailing vessels, steamers and motor vessels, the annual allowance in respect of such expenditure is computed as follows:—

- (a) where the expenditure is incurred before the expiration of 20 years of the life of the ship the normal allowance is increased by such a sum as will exhaust the expenditure over the remainder of the period for which the normal allowance will require to be made;
- (b) where the expenditure is incurred after the expiration of 20 years of the life of the ship the normal allowance is increased by the fractional part of the expenditure given in the third column of the table in paragraph 8 in next column, substituting the age of the ship when the expenditure was incurred for the "age at date of purchase."

4. The allowance in respect of refrigerating plant and insulation, except in so far as acquired with a second-hand ship (see paragraph 7) is computed separately from the allowance for the hull, etc., in order to ensure that—

- (a) the allowance ceases when the break-up value of the plant, etc., is reached, and
- (b) the aggregate allowance does not exceed the cost to the owner less the break-up value.

5. The basis for computation of the allowance in respect of the original refrigerating plant, etc., is  $9\frac{1}{2}$  per cent. (or  $5\frac{1}{2}$  per cent. in the case of sailing vessels) on the cost.

A similar allowance is made in respect of plant added to a ship (other than additions effected in the years 1917 to 1922) or for capital expenditure incurred in connection with existing plant. Where, however, the basis given in paragraph 3 is more favourable to the owner, that basis is applied, but the break-up value is computed as indicated in paragraph 6.

The allowance in respect of plant installed on a steamer or motor vessel, and delivered in one of the years 1917 to 1922, is computed on the basis of one twenty-fourth of the difference between cost and break-up value, plus  $2\frac{1}{2}$  per cent. on the cost.

6. The break-up value is computed at the rates given in paragraph 2. In the case of steamers and motor vessels equipped with refrigerating plant, etc., after the date of delivery of the ship, the rate applied is that appropriate to the year of re-delivery.

The break-up value is revised on the occasion of each extension of the existing plant, but no revision is made on account of capital expenditure on the renewal or improvement of existing plant.

7. The allowance in respect of a ship purchased second-hand is computed by reference to—

- (a) the actual cost of the ship to the new owner less the break-up value (i.e., the aggregate of the existing break-up values of the hull, etc., and refrigerating plant, etc.); and
- (b) the reasonable expectation of life of the ship at the date of purchase (see paragraphs 8 and 9).

## SHIPPING (continued)

Allowances for the hull, etc., and for refrigerating plant, etc., acquired with the ship are not separately computed.

Allowances for subsequent capital expenditure on refrigerating plant, etc., and break-up values for extensions to such plant, are separately computed on the basis given in paragraphs 5 and 6 respectively. Other capital expenditure is to be dealt with as indicated in paragraph 3.

8. As regards steamers and motor vessels, the following scale is applied except where a vessel is over 30 years old at the date of purchase; such vessels are to be dealt with according to the facts of each case.

Age at date of purchase.	Expectation of life after deducting one year.	Fractional part of cost less break-up value to be written off each year for wear and tear.
Years	Years	
0	24	1/24th
1	23	1/23rd
2	22	1/22nd
3	21	1/21st
4	20	1/20th
5	19	1/19th
6	18	1/18th
7	17	1/17th
8	16	1/16th
9	15	1/15th
10	14	1/14th
11	13	1/13th
12	12	1/12th
13	11	1/11th
14	10	1/10th
15	10	1/10th
16	10	1/10th
17	10	1/10th
18	9	1/9th
19	9	1/9th
20	9	1/9th
21	8	1/8th
22	8	1/8th
23	7	1/7th
24	6	1/6th
25	6	1/6th
26	5	1/5th
27	5	1/5th
28	4	1/4th
29	4	1/4th

9. The expectation of life of vessels other than steamers and motor vessels is determined by reference to the particular facts of each case.

SHIP AND SLIPPER MANUFACTURE		%
Engines, boilers and shafting ..	..	5
Manufacturing machinery (process plant) ..	..	10
Motor vans and lorries ..	..	20

SILK MANUFACTURE		%
Steam engines, boilers and shafting ..	..	5
General plant and machinery (including winding, throwing, doubling and weaving machinery) and electric motors ..	..	7½

<b>SILK MANUFACTURE (continued)</b>	%
Sewing, braiding and knitting machinery .. .. .	10
(The allowances are applicable to plant and machinery used in the manufacture of natural or artificial silk materials, including materials consisting partly of silk and partly of wool and/or cotton.) As regards lace, embroidery and dyeing plant and machinery, the rates laid down under those headings are to be applied.	
<b>STEAM LORRIES (see end)</b> .. .. .	15
<b>STEEL MANUFACTURE (see IRON AND STEEL).</b>	
<b>STEEL—ROLLING AND HAMMERING. STEEL RE-ROLLING</b>	
An arrangement identical with that for Iron and Steel Manufacture is applicable.	
<b>SULPHURIC ACID MANUFACTURE</b>	
<i>Chamber Process</i>	
Nitre plant, ammonia, oxidation plant, towers and plant used in connection therewith, chambers and incidental plant, chimney stack, dearsenicating plant, concentrating plant .. .. .	15
<i>Contact Process</i>	
Towers, blower, grease separating and pressure balancing chambers, heat inter-changers, pre-heaters, converters and contact mass, absorption vessels, weighing tanks and machine plant for platinisation and revivification of contact mass .. .. .	15
<i>Either Process</i>	
Plant for dealing with sulphur, raw material, mechanical and hand burners, power plant, acid eggs, storage tanks, cisterns and connections, fans, pumps, railway tank wagons .. .. .	15
(See also CHEMICAL MANUFACTURE.)	
<b>SYNTHETIC DYESTUFFS MANUFACTURE (see DYESTUFFS).</b>	
<b>TAILORING (MEN'S) (see CLOTHING—HEAVY).</b>	
<b>TAXI-CABS</b> .. .. .	20
<b>TIMBER MERCHANTS, SAW MILLERS, AND TIMBER GOODS MANUFACTURE</b>	%
Engines, boilers and main shafting .. .. .	5
General saw-milling plant and machinery .. .. .	7½
Traction engines, tractors, motor cars and haulage plant .. .. .	20
To meet war conditions, including overtime and continuous working, the rates for general saw-milling plant and machinery (but not engines, boilers and	

**TIMBER MERCHANTS, ETC. (continued)**  
*main shafting*) and for traction engines, tractors and haulage plant (*excluding motor cars*) may be increased for 1940-41 to 1946-47 inclusive to 9½ per cent. and 25 per cent. respectively.

**TOOL MANUFACTURE (see ENGINEERS' TOOLS AND MACHINE TOOLS).**

**TRACKLESS TROLLEY OMNIBUSES**  
*(see end)* .. .. . 15

#### TRAMWAYS AND LIGHT RAILWAYS

The following is an extract from the agreed scheme which is generally applied.

##### *Permanent Way.*

(Annual allowances are granted in respect of the depreciation by wear and tear of the permanent way equal to the cost of the track divided by the number of years of its estimated life.)

3. The life of the permanent way is, normally, to be taken as 12, 14 or 16 years, according to the traffic thereon. The classification is to be based on the average car mileage per mile of track per annum of the financial year preceding the year of assessment, viz:—

- (i) not exceeding 50,000 car miles per mile of track = 16 years;
- (ii) over 50,000 and not exceeding 75,000 car miles per mile of track = 14 years;
- (iii) over 75,000 and not exceeding 125,000 car miles per mile of track = 12 years;
- (iv) over 125,000 car miles per mile of track = special consideration.

Where there are special circumstances, such as exceptional gradients, the compulsory use of wood-paving, etc., tending to show that the car mileage does not fairly represent the wear and tear of the track, each such case is entitled to special consideration.

5. In determining the cost of constructing new track, or of renewing any track, there shall be excluded all expenditure on concrete foundations, and on paving except such paving as lies between the rails and extends 18 inches beyond the rails on each side, and also the cost of the land on which the track may be laid and any other expenditure of a non-recurring nature.

Provided that where a tramway authority out of the revenue of the tramway undertaking is by statute required as such authority to bear the cost of repair and renewal of a further portion of the road in addition to the portion between the rails and 18 inches beyond on each side, the cost of such repairs and renewals shall be allowed as a trading expense as and when incurred.

6. The cost of renewing concrete foundations shall be allowed as a trading expense as and when incurred, provided that if the renewed foundations are an improvement on the old, the cost of such improvement shall be excluded.

**TRAMWAYS, ETC. (continued)**

7. Renewals of special track work at junctions and crossovers so far as they do not represent improvements, shall be allowed as repairs as and when effected and shall be excluded from all claims for wear and tear.

8. Amounts received for old material whenever renewals are effected, shall be credited against the cost of the renewals, and if such old material is not disposed of at the time or is used for other purposes, the estimated value shall be credited subject to adjustment, if necessary, as and when the old material is disposed of.

9. The cost of repairs shall be allowed as an expense as and when incurred.

*Cables*

14. In addition to repairs, wear and tear is to be allowed at the rate of 3 per cent. per annum on the written down value. The value of the cables is to include the cost of laying them, but it is to exclude the cost of conduits (if any).

*Overhead Equipment, i.e., Trolley Wires and Connections*

15. No wear and tear allowance is to be made; all expenditure on maintenance and renewals should be charged as working expenses, as and when incurred.

*Cars and other Rolling Stock*

16. Subject to the ensuing clause, expenditure on maintenance and renewals is to be treated as working expenses, and allowed in lieu of wear and tear.

Wear and tear, however, should be allowed in lieu of renewals where the circumstances justify such an allowance, provided that a strict account is kept of all renewals, and that, if such renewals are charged to revenue account, they shall be shown separately in such account and added back in computing the assessable profits.

The allowance in such cases is to be 7 per cent. per annum on the written down value.

In any case, the annual expenditure on repairs is to be allowed as a deduction in computing the assessable profits.

*General Plant and Machinery*

17. All other plant and machinery, including standards, brackets, and workshop tools, but excluding loose implements, office furniture and small articles which require frequent renewal should be bulked together and wear and tear allowed thereon at the rate of 5 per cent. per annum on the written-down value, in addition to the cost of repairs.

**UNDERCLOTHING MANUFACTURE (see %  
'CLOTHING—LIGHT).****VARNISH MANUFACTURE (see PAINT).****WATER UNDERTAKINGS**

Cast iron mains	..	..	3
Asbestos air-vent mains	..	.	3
Steel mains	..	..	5
Electric plant	.	..	10
Meters	..	..	7½
Diesel engines	.	..	10
Other plant and machinery	..	.	5

An undertaking may continue to claim the renewals basis for all or any of the specified categories of plant and machinery and may defer a change to wear and tear basis for any such category to a convenient year.

**WROUGHT IRON MANUFACTURE  
(see IRON AND STEEL).****(c) Rates for Particular Types of Plant, etc., Not Confined to Specific Industries.**

ELECTRIC FURNACES	%
All parts of the furnace, including transformers, switchgear, high and low tension cable connections, furnaces, tilting gear and regulators	12½

**MOTOR LORRIES, PANTHECHNICS AND VANS, COMMERCIAL** .. 20

(Arrangement does not extend to "lit" pantechnics which are not a fixed portion of a motor.)

To meet war conditions the normal allowances may be increased by one-quarter as from 6th April, 1940, to 5th April, 1947, for vehicles operating under "A" licences or Defence Permits solely for the purpose of carrying goods for trade or industry for hire or reward. A similar increase may be allowed as from the date of commencement of abnormal conditions of running (not earlier than 6th April, 1940) for vehicles carrying goods for trade or industry and operating under:—

- (a) "B" licences or Defence Permits, partly for hire or reward within limited areas and partly for the owner's business; or
- (b) "C" licences or Defence Permits solely in connection with the owner's business where it is reasonably clear that the normal allowance is inadequate by reason of war conditions, e.g., heavier loads, increased mileage and reduced facilities for repairs.

# APPENDIX II.

671

	%		%
MOTOR OMNIBUSES .. .. .	20	ROAD ROLLERS	
A rate of 25 per cent. will be granted in respect of Bedford 32 seater (wartime) buses so long as they remain licensed to carry 32 seated passengers and such number of standing passengers as is permitted by the Regional Transport Commissioner concerned.		Steam rollers .. .	10
(See also TRACKLESS TROLLEY OMNIBUSES.)		Diesel rollers . . .	20
		Petrol rollers .. .	20
		STEAM LORRIES .. .	15
RAILWAY WAGONS OWNED BY PRIVATE TRADERS . . . . .	6½	TRACKLESS TROLLEY OMNIBUSES ..	15





## APPENDIX III.

## INCOME TAX YEAR 1947-48

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<p>S.A. Counter, Esq., 7, 654, High Street, Lowtown.</p>
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<p>Please quote File No. In any communication relating to this return</p>
<p>D Regr. No.</p>

RETURN OF INCOME OF THE YEAR 1946-47, ENDED 5 APRIL, 1947;  
AND  
CLAIM FOR ALLOWANCES FOR THE YEAR 1947-48, ENDING 5 APRIL, 1948

By virtue of the Income Tax Acts you are hereby required to prepare in Sections B, C and D (pages 2 to 5) of this form a true and correct return of all the sources of your income and of the amount derived from each source, computed in accordance with the said Acts, of the year 1946-47, ended 5 April, 1947, and to deliver such return, duly signed, to me within 21 days from this date.

You should also complete pages 6, 7 and 8, so far as applicable to your case, to enable you to obtain any allowances to which you are entitled for the Income Tax year 1947-48, ending 5 April, 1948.

For guidance in filling up the form, notes are given in the enclosure and references to the appropriate notes will be found in each Section of the form.

The following instructions apply to exceptional cases—

- (1) Return made elsewhere.—Fill up Section A only.
- (2) Individual not domiciled in, or British subject not ordinarily resident in, the United Kingdom of Great Britain and Northern Ireland.—Fill up Section P only.
- (3) Individual resident in Eire and not resident in the United Kingdom.—See Note I of enclosure.
- (4) Return by a Partner.—(a) Partnership income included in Firm's return: omit from Section B but include in Section C.  
(b) Personal income: if not taxed at the source, include in Section B; if taxed at the source, include in Section C.
- (5) Return by an individual chargeable to Sur-tax.—Apply for the special sheet of notes applicable to such a case if not already enclosed.

If you wish for any further information, you should apply to me

Date

Section

A

Declaration that a full return has been made elsewhere

I have already made the return required by this form from my <sup>\*business address, namely—</sup>  
<sup>\*private residence,</sup>

Full description of Firm, in case of a Partner

Name of Employer, in case of an Employee

Signature

\* Delete as necessary

No. 11

The names and addresses on this Form are fictitious

Y

**Section  
B**
**STATEMENT OF ALL INCOME NOT TAXED AT THE SOURCE**

Enter the word "None" in any of the spaces below which  
Enter the following in Section C and not in Section B:—Dividends, interest, annuities, etc., subjected to  
Income Tax under Schedule A; and income from occupation of land

Classes of Income and General Directions—including references to Notes in the Enclosure

**TRADE, PROFESSION OR VOCATION**

How profits to be computed See Note 2.

Include, as separate items, income from farming assessable under Schedule D and income from market gardening. See Note 23.

If a balancing charge arises (see Note 15), enter it in the space for "Other Profits or Income" below

Deductions in respect of—

(a) machinery or plant See Note 3.

(b) industrial buildings, mining assets, patent rights and scientific research. See Note 3.

(c) losses. See Note 4.

**OFFICE, EMPLOYMENT OR PENSION**

Enter name and address of employer, nature of appointment, the full earnings (including any commissions, bonus, percentage of profits, income tax on the emoluments borne by the employer, etc.) and particulars of any deductions claimed for expenses (see Note 5). Give details of any directors' fees.

Include all casual fees or payments for services, but omit any Wounds, Disablement or Disability Pension mentioned in Note 6.

**INTEREST, DIVIDENDS, ANNUITIES AND OTHER ANNUAL PAYMENTS, NOT SUBJECTED TO UNITED KINGDOM INCOME TAX AT THE SOURCE**

For information as to certain dividends and interest not taxed at the source, see Note 7.

Include, as separate items, any income from Manorial Dues, Fines, etc., and Payments in lieu of, or compositions for, Tithes. See Note 8.

**DOMINION AND FOREIGN SECURITIES AND POSSESSIONS, NOT SUBJECTED TO UNITED KINGDOM INCOME TAX AT THE SOURCE**

Income from Securities and Possessions other than from Trade, etc., referred to below

Enter the amount that arose in the year, whether or not received in the United Kingdom. See Note 9 (a) & (b).

As to income from lands, houses, etc., occupied in Eire, see Note 9 (c).

Income immediately derived from Trade, Profession or Vocation carried on by the taxpayer solely or in partnership, or arising from any Office, Employment or Pension—

(a) Arising elsewhere than in Eire.—Enter the full amount received in the year in the United Kingdom and see Note 9 (d)

(b) Arising in Eire—see Note 9 (e).

**Estate of Deceased Persons**

Enter here any income from a "foreign estate"—see Note 10.

**INCOME, NOT TAXED AT THE SOURCE, RECEIVABLE BY A COMPANY, TRUST, ETC., ABROAD, in the circumstances referred to in Note 11**

Give particulars and amount.

**INCOME, NOT TAXED AT THE SOURCE, UNDER SETTLEMENTS, ETC., such as are mentioned in Note 12**

Give particulars and amount

**OTHER PROFITS OR INCOME, NOT TAXED AT THE SOURCE**

Include family allowances under the Family Allowances Act, 1945, "excess rents" of lands, houses, etc., in the United Kingdom (see Note 14), balancing charges on sale of assets, etc. (see Note 15), sale of patent rights (see Note 16), or income involved in transactions of the nature referred to in Note 13

Give particulars of all profits or income not taxed at the source and not falling under any of the above heads. See Note 17.

**WIFE'S INCOME, NOT TAXED AT THE SOURCE, IF NOT ALL INCLUDED ABOVE**

State the sources and amounts, according to the appropriate directions above

As to liability of husband to include his wife's income, see Note 18

If, since 5 April, 1946, there have been any alterations in the sources of income, not taxable by deduction, of the taxpayer (or his wife), give full particulars of the alterations opposite (see Note 19). As regards alterations in holdings of Government securities, the interest on which is received without deduction of tax, include the name of the security, the rate of interest, the amount of the holding newly acquired or disposed of, and the date of acquisition or disposal.

## OF THE YEAR 1946-47, ENDED 5 APRIL, 1947

relate to the heads under which you had no income

United Kingdom Income Tax before receipt; income from property in the United Kingdom assessable to in the United Kingdom assessable to Income Tax under Schedule B

Enter particulars of each source and the amount derived therefrom	£	s.	d.
The Trade, Profession or Vocation of..... <u>Grocer</u> carried on by..... <u>me</u> ..... at..... <u>7654, High Street,</u> <u>Lewtown</u> ..... Enter here amounts (if any) claimed for any deductions under heads (a) and (b) opposite. The amounts claimed under each head should be distinguished (a) Wear and Tear..... <u>324</u>	2,300	-	-
Office, Employment or Pension, viz.— <u>Director, Lewtown Wholesalers, Ltd.</u> <u>Lewtown Buildings, Lewtown</u> ..... Fees <u>£500</u> <u>Less: Expenses as agreed</u> ..... <u>25</u>	475	-	-
Interest or Dividends on War Loan (not subjected to United Kingdom Income Tax at the source), viz.— <u>£2,000 3½% War Loan</u>	70	-	-
Interest on Bank (including Post Office or other Savings Bank) accounts or deposits..... <u>F.O.S.B.</u>	5	-	-
Discounts on Treasury Bills..... Other Interest, Dividends, Annuities, Annual Payments, etc. (not subjected to United Kingdom Income Tax at the source), viz.— <u>£1,000 3% Defence Bonds</u>	30	-	-
Dominion and Foreign Securities and Possessions, viz.—	1	0	0
Income receivable by a Company, Trust, etc., abroad (see opposite)		N	O
Income under Settlements, etc. (see opposite)		N	O
Family Allowances under the Family Allowances Act, 1945, for..... children..... "Excess Rents" (see opposite)..... <u>Rent of Sansouci £75 N.A.V. £40</u> <u>Seaside, Bexhill</u>	Not Claimed		
Letting Furnished House at..... Underwriting (or Sub-Underwriting) Commissions..... Any other profits or income, not taxed at the source, viz.—	20	-	-
Wife's income, not taxed at the source and not already entered above, viz.— <u>Wages from my business</u>	45	-	-
Wife's income, not taxed at the source and not already entered above, viz.— <u>Wages from my business</u>	130	-	-
Particulars of alterations in sources of income (not taxable by deduction), since 5 April, 1946— <u>£1500 War Loan bought 20.4.46</u>			

[PLEASE TURN OVER

## STATEMENT OF ALL INCOME TAXED AT THE SOURCE

Section  
C

Income in respect of which Income Tax is payable directly and not by deduction, and all income from office or employment, and all income from occupation of land assessable under Schedule B, and all income from other sources, including income from the sale of land, and all income from the occupation of land assessable under Schedule B, should be entered in the spaces (a) to (h) which relate to the heads under which the income is received. Enter the word "None" in any of the spaces (a) to (h) which relate to the heads under which the income is received if under any head there is insufficient space, enter the particulars on a separate sheet and carry the total to the total column.

Classes of Income and General Directions—including references to Notes in the Enclosure

(a) PARTNERSHIP INCOME. See Note 21.

(b) (i) OWNERSHIP OF LAND, HOUSES, ETC., in the United Kingdom

Enter description of property, name of occupier, precise address and the income therefrom reckoned as directed in Note 22. Include the net annual value of any property occupied by and belonging to yourself or your wife. Where a property has been purchased or sold since 5 April, 1946, enter date of purchase or sale.

(ii) LAND, HOUSES, ETC., which you occupy rent free or at a rent less than the net annual value. See Note 22 (b).

(c) OCCUPATION OF LAND in the United Kingdom assessable under Schedule B

Enter description, name (if any) and situation of the land, and the income therefrom reckoned as directed in Note 23. Include any lands occupied which are owned by yourself or your wife, and any amenity lands (e.g., parklands and woods).

(d) DIVIDENDS, INTEREST, ANNUITIES & OTHER INCOME SUBJECTED TO UNITED KINGDOM INCOME TAX AT THE SOURCE

Enter the gross amount receivable in the above year in respect of each source. See Note 24 (a). Dividends declared "free of tax", or paid without deduction of tax, must be entered here, the amounts to be entered being the gross amounts corresponding to the net amounts receivable. It should be plainly shown whether tax has or has not been added to the net amounts. See Note 24 (a).

Include here, as separate items, the value of any "funding bonds" (see Note 9 (a)) taxed before receipt, any income from the estate of a deceased person if a "United Kingdom estate" (see Note 10), and income (taxed at the source) involved in transactions of the nature referred to in Note 13. As regards vouchers, see Note 24 (b).

(e) INTEREST FROM BUILDING SOCIETIES

Give names of Societies and enter the actual amounts received or credited.

(f) INCOME, TAXED AT THE SOURCE, RECEIVABLE BY A COMPANY, TRUST, ETC., ABROAD, in the circumstances referred to in Note 11

Give particulars and state the gross amount receivable in the above year—see Note 24 (a).

(g) INCOME, TAXED AT THE SOURCE, UNDER SETTLEMENTS, ETC., such as are mentioned in Note 12

Give particulars and state the gross amount. In the case of a capital sum treated as income of the settlor in the circumstances referred to in Note 12 an addition for tax is to be made to the amount actually received. See Note 24 (a).

(h) WIFE'S INCOME, TAXED AT THE SOURCE, IF NOT ALL INCLUDED ABOVE

State the sources and the gross amounts according to the appropriate directions above. See Note 18.

If all included above, state "Included above", or if none, state "None".

Section  
D

## STATEMENT OF GROUND RENT, INTEREST, ETC.,

## General Directions

(i) Enter in the space opposite particulars of all Charges payable out of the income, such as Ground Rents, Rents under leases granted for a term exceeding fifty years, Interest on Mortgages or Loans, Annuities, Patent Royalties, or other Annual Payments, including Payments under a Court Order or Agreement made binding by deed or otherwise. Where Income Tax is deducted on payments, the amount to be entered is the gross amount. See Note 26.

If there are no such charges, state "None". The space opposite should NOT be left blank.

Omit Life Insurance Premiums from this Section, but enter them in Section N (page 8).

(ii) If, since 5 April, 1946, there has been any alteration in the annual amount of any Charge, or any new Charge has become payable, particulars should be given hereunder.

(iii) Particulars of such alterations (with the dates) since 5 April, 1946—

I declare that, to the best of my judgment and belief, the statements in Sections B, C and D of this form contain a true and accurate statement of the facts and figures required by the provisions of the Income Tax Acts.

(If you desire my assessment upon you under Schedule D to be made by the Special Commissioners (see Note 20), write "Yes" here.

If you make the return as Executor, Trustee, Agent, Receiver, Factor, etc., state in what capacity and for whom made.

Given under my hand this.....

DECLARATION WHICH MUST

# **SOURCE OF THE YEAR 1946-47, ENDED 5 APRIL, 1947**

Income, employment or pension, should be entered in Section B and not in Section C. All income from ownership of property should be included in Section C and not in Section B.

If you had no income

fill appropriate space below

Enter particulars of each source and the amount derived therefrom		£	s.	d.		
(a)			N	O	N	E
(b)	Mihus, New Road, Loughton	60	-	-		
	Seaside, Bexhill	30	-	-		
	Seaside, Bexhill	40	-	-		
	7654, High Street, Loughton	220	-	-		
(c)			N	O	N	E
(d)	Per attached schedule (not reproduced) (includes dividend from South African English Houses, Ltd. on which U.K. rate 5/6d.)	615	-	-		
(e)			N	O	N	E
(f)			N	O	N	E
(g)			N	O	N	E
(h)		Included above				
TOTAL OF INCOME TAXED AT THE SOURCE		965	-	-		

## **PAYABLE IN THE YEAR 1946-47, ENDED 5 APRIL, 1947**

Description of Charges		Gross amounts payable in above year		
		£	s.	d.
(i) Ground Rent on	Seaside, Bexhill	2	-	-
Interest on Mortgage or Loan—			N	O
£ at % on			N	E
payable to				
£ at % on				
payable to				
Annuities and other Annual Payments, including Payments under a Court Order or Agreement made binding by deed or otherwise, viz—	Bank Interest	96	2	6
payable to	Barclays Bank Ltd. per enclosed certificate			
TOTAL OF CHARGES		98	2	6

### **BE COMPLETED AND SIGNED**

Set return of all the sources of my income and of the amount derived from each source of the year ended 5 April, 1947, computed in

15th day of May, 1947.

(Signed) Silas Albert Counter

Mihus, New Road, Loughton, Private Residence(s)

Signature (in full)

NOTE—If a woman, state whether widow, spinster or married

(PLEASE TURN OVER)

## CLAIM FOR ALLOWANCES FOR THE

**Section E** **ALLOWANCE TO A MARRIED MAN** in respect of his wife [See Note 30]

Full Christian names of my wife who is living with me, or is wholly maintained by me .. 17-22

If you were married after 5 April, 1946, state date of marriage and your wife's maiden name ..

**Section F** **ALLOWANCE TO A WIDOWER OR WIDOW** in respect of female relative resident with him or her, or in respect of other female person resident with and employed by him or her, for the purpose stated below [See Note 31]

Name of female relative resident with me, or of other female person resident with and employed by me, either in the capacity of a housekeeper, or for the purpose of having the charge and care of any child or adopted child of mine in respect of whom the allowance for children is given

Whether she is "married," "widow," or "spinster" (If married, but living apart from her husband, state so)

Relationship (if any) to me or to my deceased wife (or husband) If no relative is available, state so

Surname	Full Christian Names		

**Section G** **ALLOWANCE TO AN UNMARRIED PERSON** in respect of mother or other female relative maintained by and living with the claimant for the purpose stated below [See Note 32]

Name of mother, or other female relative, living with and maintained by me, for the purpose of having the charge and care of any brother or sister of mine in respect of whom the allowance for children or adopted children is given

Whether she is "married," "widow," or "spinster" (If married, but living apart from her husband, state so)

Relationship to me

Does any other relative contribute to her maintenance?

Surname	Full Christian Names			

**Section H** **ALLOWANCE TO A MARRIED MAN WHO IS ENTITLED TO THE PERSONAL ALLOWANCE OF £180** and whose wife is totally incapacitated by physical or mental infirmity, in respect of a female person resident with and maintained or employed by him for the purpose stated below [See Note 33]

Name of female person resident with and maintained or employed by me for the purpose of having the charge and care of any child resident with me in respect of whom I am entitled to the allowance for children

Nature of wife's total incapacity

From what date, if after 5 April, 1946, has your wife been totally incapacitated?

Do you expect that your wife will be totally incapacitated during the whole of the year ending 5 April, 1948?

Surname	Full Christian Names			

**Section J** **ALLOWANCE TO A TAXPAYER WHO IS NOT ENTITLED TO THE PERSONAL ALLOWANCE OF £180**, in respect of a female person resident with and maintained or employed by the claimant for the purpose stated below [See Note 34]

Name of female person resident with and maintained or employed by me for the purpose of having the charge and care of any child resident with me in respect of whom I am entitled to the allowance for children

If the claimant is a woman and is totally incapacitated by physical or mental infirmity

If the claimant is a woman and is in full-time employment or business

What is the nature of your total incapacity, and from what date, if after 5 April, 1946, have you been totally incapacitated?

Do you expect that you will be totally incapacitated during the whole of the year ending 5 April, 1948?

On what date, if after 5 April, 1946, did your full-time employment or business commence?

Do you expect to be in full-time employment or business during the whole of the year ending 5 April, 1948?

Surname	Full Christian Names				

YEAR 1947-48, ENDING 5 APRIL, 1948

[See Note 27]

Section  
**K**

## ALLOWANCE in respect of CHILDREN

[If any child is a step-child, state so. As to adopted children, see Note 35]

If the parents of a child are divorced or separated, the fact should be stated. In those and certain other cases—see Note 35—the allowance is apportionable

[See Note 35]

Name of each child or step-child who is living and under the age of 16 years at any time within the year ending 5 April, 1948, or who, if over that age on 6 April, 1947, is receiving full-time instruction at an educational establishment or is required to devote full time for not less than two years to training for a trade, profession or vocation

Date of Birth

Has the child any earnings or other income in own right? If so, state annual amount, excluding scholarship income

In the case of children over the age of 16 years on 6 April, 1947—Name and address of educational establishment or Name and address of employer by whom the child is undergoing training and nature of trade, etc., for which the child is being trained

Where allowance apportionable (see above), proportion claimed by me

Surname	Full Christian Names	Day	Month	Year	Has the child any earnings or other income in own right? If so, state annual amount, excluding scholarship income	In the case of children over the age of 16 years on 6 April, 1947—Name and address of educational establishment or Name and address of employer by whom the child is undergoing training and nature of trade, etc., for which the child is being trained	Where allowance apportionable (see above), proportion claimed by me
Counter	John Andrew	15	6	30	No	Wellknown School.	
Counter	Maria	12	8	32	No		
Counter	William Henry	4	1	37	No		

Section  
**L**

## ALLOWANCE in respect of (I) DEPENDENT RELATIVES maintained by the claimant or (II) RELATIVES denied unemployment allowance or public assistance or (III) DAUGHTER upon whose services the claimant is compelled to depend by reason of old age or infirmity

[See Note 36]

## (I) CLAIM IN RESPECT OF RELATIVES MAINTAINED BY THE CLAIMANT

Name of relative maintained at my own expense and incapacitated by old age or infirmity from maintaining himself or herself, or name of widowed mother maintained at my own expense

Relationship to me or to my wife (or husband), if widowed mother, state so

Date of Birth

Annual income of the relative from all sources, excluding voluntary contribution

Nature of infirmity, if any

Where now residing? If not with you, state the annual amount of your contribution

Amount contributed by other relatives, if none state "None"

Surname	Full Christian Names	Day	Month	Year	Annual income of the relative from all sources, excluding voluntary contribution	Nature of infirmity, if any	Where now residing? If not with you, state the annual amount of your contribution	Amount contributed by other relatives, if none state "None"
---------	----------------------	-----	-------	------	--	-----------------------------	---	---

## (II) CLAIM IN RESPECT OF RELATIVES DENIED UNEMPLOYMENT ALLOWANCE, ETC.

Name of relative denied, wholly or in part, unemployment allowance or public assistance on the ground that he or she is maintained wholly or partly by me

Relationship to me

Whether living with me

Which is denied (a) unemployment allowance, or (b) public assistance

Amount deemed to be paid by me towards the maintenance

Surname	Full Christian Names	Relationship to me	Whether living with me	Which is denied (a) unemployment allowance, or (b) public assistance	Amount deemed to be paid by me towards the maintenance
---------	----------------------	--------------------	------------------------	--	--

## (III) CLAIM IN RESPECT OF DAUGHTER

Name of daughter maintained by me and upon whose services I am compelled to depend by reason of old age or infirmity

Whether she is "married," "widow," or "spinster." (If married, but living apart from her husband, state so)

Whether resident with me

If you depend on her services on account of old age, state age. If infirmity, state nature of infirmity

Surname	Full Christian Names	Whether she is "married," "widow," or "spinster." (If married, but living apart from her husband, state so)	Whether resident with me	If you depend on her services on account of old age, state age. If infirmity, state nature of infirmity
---------	----------------------	---	--------------------------	---

Section  
**M**

## ALLOWANCE in respect of INCOME OTHER THAN EARNED INCOME, where either the claimant or his wife living with him was on 6 April, 1947, 65 years of age or more, and the total income does not exceed £500 by too great an amount

[See Note 29]

Name of claimant, if 65 years of age or more, or of his wife, if 65 years of age or more and living with him

Date of Birth

Surname	Full Christian Names	Day	Month	Year
---------	----------------------	-----	-------	------

[PLEASE TURN OVER]



## CLAIM FOR ALLOWANCES (Continued)

Section <b>N</b>		ALLOWANCE in respect of LIFE INSURANCES or contracts for deferred annuities on the life of claimant or his wife				[See Note 39]
State whether the Insurance or Annuity is on the life of Self or Wife	Name of Insurance Company or Friendly Society, etc.	Date of Policy or Contract if before 23 June 1916 or after 5 April 1946	*CAPITAL SUM PAYABLE AT DEATH—excluding bonus or any other additional benefit	Amount of Premiums to be paid in the year ending 5 April 1948		
Self	Grocers Own		£ 2,000	75	-	
Wife	do.		£ 2,000	120	-	
			TOTAL	195	-	

(\*) No CAPITAL SUM is payable at Death, state particulars of the Policy

Section <b>O</b>		OLD AGE ETC. PENSIONS CONTRIBUTIONS		[See Note 37]
If you are or your wife is a compulsory contributor under the Widows' Orphans' and Old Age Contributory Pensions Acts, state which of you contributes				
If either of you is a voluntary contributor, state the weekly amount of your contribution .....				
If you pay contributions in respect of any personal or domestic employee, see Note 37				

## DECLARATION TO BE SIGNED IF ANY ALLOWANCES (specified in Notes 28 to 39 of the enclosure) ARE CLAIMED

I declare that all the particulars given by me in Sections E to O in respect of the year ending 5 April, 1948, are truly and correctly stated to the best of my judgment and belief, and that no other individual is entitled to relief from Income Tax for any female relative in respect of whom I have claimed an allowance in Section F or G, or if any other individual is so entitled that such individual has relinquished his or her claim to the allowance. I claim the reliefs to which I am entitled by reason of the facts stated in Sections B to O

Dated this 15th day of May 1947.

(Signed) S. A. Coulter ..... Signature

Section **P** Declaration to be made by an individual not domiciled in, or by a British subject not ordinarily resident in, the United Kingdom of Great Britain and Northern Ireland [See page 1]

I am { <sup>\*not domiciled in</sup> a British subject not ordinarily resident in } the United Kingdom, and I request that a form appropriate to my case may be sent to me.

(\* Strike out the words not applicable)

..... Signature

..... Private Residence

..... 194

## PENALTIES

The penalty for neglecting to make a return, or for making an untrue or incorrect return, is a sum not exceeding £20 and treble the tax chargeable. A penalty not exceeding £5 may be imposed for neglecting to make a return, even though the person proceeded against may prove that he was not chargeable to Income Tax.

The penalty for fraudulently concealing or untruly declaring any particulars in making any claim for any allowance or deduction is £20 and treble the tax chargeable in respect of all the sources of income.

If any person, for the purpose of obtaining any allowance, reduction, rebate, or repayment in respect of Income Tax, either for himself or for any other person, or in any return made with reference to Income Tax, knowingly makes any false statement or false representation, he is liable, on summary conviction, to imprisonment for a term not exceeding six months with hard labour.

## APPENDIX IV.

## RATING AND VALUATION ACT, 1925.

24. (1)—For the purpose of the making or revision of valuation lists under this part of this Act, the following provisions shall have effect with respect to the valuation of any hereditament other than a hereditament, the value of which is ascertained by reference to the accounts, receipts or profits of the undertaking carried on therein :—

- (a) All such plant or machinery in or on the hereditament as belongs to any of the classes specified in the Third Schedule to this Act shall be deemed to be a part of the hereditament.
- (b) Subject as aforesaid no account shall be taken of the value of any plant or machinery in or on the hereditament.

## THIRD SCHEDULE.

## CLASSES OF MACHINERY AND PLANT TO BE DEEMED TO BE A PART OF THE HEREDITAMENT.

(1)—Machinery and plant (together with the shafting, pipes, cables, wires and other appliances and structures accessory thereto) which is used or intended to be used mainly or exclusively in connection with any of the following purposes :—

- (a) The generation, storage, primary transformation or main transmission of power in or on the hereditament, or
- (b) The heating, cooling, ventilating, lighting, draining or supplying of water to the land or buildings of which the hereditament consists, or the protecting of the hereditament from fire :

Provided that in the case of machinery or plant which is in or on the hereditament for the purpose of manufacturing operations or trade processes, the fact that it is used in connection with those operations or processes for the purpose of heating, cooling, ventilating, lighting, supplying water or protecting from fire shall not cause it to be treated as falling within the classes of machinery or plant specified in this Schedule.

(2)—Lifts and elevators mainly or usually used for passengers.

(3)—Railway and tramway lines and tracks.

(4)—Such part of any plant or any combination of plant and machinery, including gas holders, blast furnaces, coke ovens, tar distilling plant, cupolas, water towers with tanks, as is, or is in the nature of a building or structure.

## APPENDIX V.

## BANKRUPTCY REGULATIONS.

## CLAIMS FOR TAXES.

Regulations as to the treatment in bankruptcy of claims for taxes agreed between the Board of Trade and the Commissioners of Inland Revenue. These are to be substituted for the provisions of paragraph 20 of Tr. Circular No. 4, which is issued to every trustee in bankruptcy on his appointment.

1.—Proofs may be made for the full amount of income tax and sur-tax assessed upon the debtor at the date of the receiving order for the year of assessment ending 5th April next after that date and such tax will rank for dividend.

2.—Proofs may be made for income tax and sur-tax (including super-tax), assessed upon the debtor at the date of receiving order for a year or years prior to that in which the order is made and such tax will rank for dividend except so far as it is tax payable in priority under Section 33 (1) of the Bankruptcy Act, 1914.

3.—Proofs may be made for land tax assessed upon the debtor at the date of the receiving order and such tax will rank for dividend except so far as it is tax payable in priority under Section 33 (1) of the Bankruptcy Act, 1914. Provided that where the receiving order was made prior to 1st January in the year of assessment, proofs will not be made, or, if made, will be withdrawn, if on the said 1st January the property in respect of which the land tax is assessed is occupied by a person other than the debtor or the trustee in bankruptcy.

4.—(a) When the receiving order is made on or after 6th April in any year but before a resolution has been passed by the House of Commons in Committee of Ways and Means imposing income tax and sur-tax for the year commencing on such 6th April, and having statutory effect under the Provisional Collection of Taxes Act, 1913, no proof will be made for any income tax or sur-tax for that year.

(b) Proofs may be made for any tax imposed at the date of the receiving order, although the assessment of such tax may be made subsequently to the date of the order. The tax will rank for dividend except so far as it is tax payable in priority under Section 33 (1) of the Bankruptcy Act, 1914. In the case of sur-tax imposed at the date of the receiving order at a rate to be determined by Parliament thereafter, proof may be made on the basis that the existing rates of sur-tax are re-imposed. In the event of the liability being ultimately altered an amended proof will be lodged.

5.—(a) Where proof has been made for income tax assessed upon the debtor under Schedules B, D, or E, and it is claimed that the debtor had no income taxable under such schedules, or that the assessments are excessive, an affidavit by the debtor setting out the grounds of claim accompanied by a certificate by the trustee in the bankruptcy in the terms of the First Schedule to these Regulations may be submitted and upon receipt thereof the Inland Revenue Authorities will forego so much of the claim as appears to them on an examination of the said affidavit and certificate to be excessive. The form to be used for the purpose of such claim may be obtained from the Inspector of Taxes upon application.

(b) In cases where an affidavit by the debtor cannot be obtained, a certificate by the trustee in bankruptcy may be submitted, but the reason for the failure to furnish an affidavit must be stated in the certificate.

(c) Claims to relief from tax on account of "Personal Allowance" or such other reliefs and allowances as under the Income Tax Acts are dependent upon a statement of total income should be made *by the debtor* in the ordinary manner upon forms of declaration which may be obtained for the purpose from the office of any Inspector of Taxes.

In cases where such claims and statements cannot be obtained from the debtor, the Inland Revenue may, in lieu thereof, accept a certificate from the trustee in bankruptcy setting forth the relevant facts and may allow such relief as they are satisfied could properly have been claimed by the debtor.

(d) Any waiver of claim under sub-paragraphs (a) and (b) of this Regulation shall not extend to tax which the debtor was entitled to deduct from any interest of money, annuities, royalties or other sums paid in respect of the user of a patent or copyright, or other annual payments.

6.—Where a Collector of Income Tax has levied a distress on the goods of a debtor before the making of a receiving order, the following conditions shall apply:—

- (i) If the distress has been completed by the sale of the goods distrained prior to the making of the receiving order, the collector shall retain the proceeds of sale, so far as the same are necessary to satisfy the amount for which distress was levied.
- (ii) If the distress has not been so completed, the collector will withdraw upon receipt of an undertaking by the Official Receiver or Trustee in the terms of the Second Schedule to these Regulations to treat such sum as may be legally due to the collector under and by virtue of the distress as a charge on the proceeds of the goods distrained on.

Notes:—

- (a) If the distress has been levied within three months next before the date of the receiving order the goods or proceeds will be subject to the charge imposed by Section 33 (4) of the Bankruptcy Act, 1914.
- (b) If an available act of bankruptcy has been committed by the debtor prior to the levying of the distress, nothing will be due to the collector under and by virtue of the distress, and he will prove in the bankruptcy for the debt for taxes for which the distress was levied but make no claim in respect of the costs of the distress.

## FIRST SCHEDULE.

CLAIM FOR RELIEF FROM ASSESSMENTS OF INCOME TAX UNDER  
SCHEDULES B, D OR E.*The Bankruptcy Acts, 1914 and 1926*Court..... No. of Matter.....  
Re .....  
of .....I,.....the above-named debtor, do hereby make  
oath and say as follows :—

That I am justly and truly entitled to be relieved from the payment  
of the sum of £ ..... being the tax payable under the assessment  
upon me under Schedule.....for the year(s) from 6th April  
.....to 6th April.....on the following grounds :—  
(Here specify the grounds of claim.)

Sworn at  
this ..... day of ..... , 19 ..  
Before me.....

## CERTIFICATE.

I hereby certify that from an examination of the above-named debtor  
(against whom a receiving order was made on the ..... day of  
19 .. ) and from such evidence, books, accounts, etc., as have been produced  
to me, it appears that if the debtor had availed himself of the statutory  
provisions for relief there would have been \*no less liability to income tax  
and that, therefore, the debtor and his estate should be relieved accordingly.

(Signed).....  
Trustee.

Dated this ..... day of ..... , 19 ..  
\* Strike out as appropriate.

*Note I.*—Any waiver of claim in consequence of the above certificate will  
not extend to tax which the debtor was entitled to deduct from any interest  
of money, annuities, royalties or other sums paid in respect of the user of a  
patent or copyright, or other annual payments.

*Note II.*—The evidence in support of the claim for relief should be attached  
to this certificate.

## SECOND SCHEDULE.

## UNDERTAKING AS TO PAYMENT OF TAXES IN CASES OF DISTRESS.

*The Bankruptcy Acts, 1914 and 1926.*

Re .....

In consideration of your forbearing to realise and withdrawing from  
possession under the distress which you have levied or caused to be levied  
upon such goods of the above-named debtor as are liable to a distress for  
taxes in arrear due from such debtor, I HEREBY UNDERTAKE (without  
prejudice to the rights of preferential creditors under Section 33 (4) of the  
Bankruptcy Act, 1914) to treat the amount of money for which such distress  
is available, including the costs which you have incurred in the above levy,  
as a first charge on the net proceeds of any realisation of such goods which  
may come into my hands, subject only to the rights of such preferential  
creditors as aforesaid.

Dated this ..... day of ..... , 19 ..  
(Signed) .....

Official Receiver.

Address .....

To.....

## INCOME TAX RETURNS MADE BY BANKRUPTS.

A trustee in bankruptcy is not entitled to require the disclosure to him of particulars shown in any returns furnished by a bankrupt for income tax purposes. The Board of Inland Revenue, have, however, agreed, as a result of negotiations with the Board of Trade, that copies of returns rendered by a bankrupt may be supplied to a trustee provided he furnishes a specific authority in the terms of the draft attached, signed by the bankrupt. A trustee should avail himself of these facilities only in cases in which reasonable grounds exist for supposing that the returns made by the bankrupt contain information of practical importance.

To H.M. Inspector of Taxes, .....19 .....

..... District.

I have to inform you that on .....  
a Receiving Order in Bankruptcy was made against me in the .....  
Court. . I hereby authorise and request you to supply to the trustee of my  
estate, Mr..... of .....  
copies of the returns made by me of my income for income tax purposes for  
the undermentioned years :—

Year ending 5th April, 19.....

" " " " 19.....

" " " " 19.....

Signature .....

Address .....

.....

## APPENDIX VI.

## NOTES ON TAXATION IN EIRE.

	1927-28 to 1931-32, 3/- 3/6	1932-33 and 1933-34, 5/-	1934-35 to 1938-39, 4/6	1939-40, 5/6	1940-41, 6/6	1941-42 to 1943-44, 7/6	1944-46, 7/6	1946-48 6/6
(a) Standard Rate ..	£225	£100	£100	£100	£100	1939-40, 1939-40.		
Reduced Rate Relief— Half Rate on ..								

## Allowances :—

Earned Income ..  $\frac{1}{10}$ th (max. £200).  $\frac{1}{10}$ th of 1st £450  $\frac{1}{10}$ th (max. £300).  
 (max. £200).

Personal—Single  
 Married  
 Additional Per-  
 sonal on Wife's

Earned Income £135  
 225

£125  
 225

do.  
 do.

(b) Child—one ..

£36

$\frac{1}{10}$ ths (max. £45).  $\frac{1}{10}$ ths (max. £45).  
 £50 each, increased  
 to £60 in 1939-37.

do.  
 £60<sup>†</sup>  
 48<sup>†</sup>

(c) Housekeeper ..  
 Dependant Rela-  
 tive .. ..

27  
 45  
 25  
 none.

£45  
 25  
 none.

do.  
 do.

(a) From 1927-1931 the standard rate was 3/-.

(b) Child must be living at beginning of tax year. Child's income must not exceed £40.

(c) Housekeeper must be for purpose of looking after child.

For 1930-31 onwards, the preceding year basis has replaced the average system. Cases IV and V of Schedule D are abolished, and the sources included in Case III, all income assessable thereunder being aggregated, except those items which are on the remittances basis, cattle and milk dealers profits, and certain other items. Remittances basis is limited to persons not domiciled in Eire and Eire citizens not ordinarily resident therein, and certain investments of assurance companies. The Repairs Allowance under Schedule A was abolished in Eire for 1934-35 onwards except in regard to (a) Lands and Farm Buildings, etc., (b) Mills, Factories, etc., and (c) Small Cottage Property. Profit rentals of business premises are assessed under Case III. For 1933-34 onwards, doubly resident persons spending more than six months in fiscal year in Eire can claim further relief from Eire tax, but not more than will reduce total tax (including Sur-tax) paid in both countries to amount they would have paid if not resident in Eire.

\* 1st and 2nd child £60 each.

† 3rd and later child £43 for 1945-46.

## SUR-TAX.

1931-32 to 1937-38.					s.	d.
First	£1,500	..	..	..	..	nil.
Next	£500	..	..	..	..	6 in £.
	1,000	..	..	..	..	1 0
	1,000	..	..	..	..	1 9
	1,000	..	..	..	..	2 6
	1,000	..	..	..	..	3 3
	2,000	..	..	..	..	4 0
	2,000	..	..	..	..	4 9
	10,000	..	..	..	..	5 6
	remainder	..	..	..	..	6 3

For 1938-39 all rates on incomes exceeding £3,000 and not exceeding £8,000, were increased by 10%, and rates on incomes exceeding £8,000 are increased by 15%.

For 1939-40 to 1945-46, the increases are :—

Income exceeding	£3,000	..	..	10%
"	"	£8,000	..	15%
"	"	£20,000	..	20%

Marginal relief—

Where the statutory total income only slightly exceeds £3,000 (or £8,000 or £20,000) (as the case may be), the Sur-tax payable is not to exceed the sum of the following :—

- (a) The amount of the Sur-tax on an income of £3,000 (or £8,000 or £20,000); and
- (b) The amount by which the income exceeds £3,000 (or £8,000 or £20,000) reduced by Income Tax at the standard rate on such excess.

For 1946-47 the rates are :—

					s.	d.
On First	£1,500	..	..	..	..	Nil
„ next	£500 to	£2,000	..	..	..	9 in £
„	£1,000 „	£3,000	..	..	..	1 6
„	£1,000 „	£4,000	..	..	..	3 0
„	£1,000 „	£5,000	..	..	..	4 0
„	£1,000 „	£6,000	..	..	..	5 0
„	£2,000 „	£8,000	..	..	..	6 0
„	£2,000 „	£10,000	..	..	..	7 6
„	£10,000 „	£20,000	..	..	..	8 0
On any excess over	£20,000	..	..	..	..	8 6

SUPER-TAX 1927-28 AND 1928-29; SUR-TAX 1927-28 to 1930-31.

					s.	d.
First	£2,000	..	..	..	..	nil.
Next	500	..	..	..	..	9
	500	..	..	..	..	1 0
	1,000	..	..	..	..	1 6
	1,000	..	..	..	..	2 3
	1,000	..	..	..	..	3 0
	2,000	..	..	..	..	3 6
	2,000	..	..	..	..	4 0
	remainder	..	..	..	..	4 6



**Excess Sur-tax 1941-42 onwards.**

Where for either 1941-42 or 1942-43, the total income of an individual resident in Eire exceeds £1,500 and includes profits of a trade or business carried on by him (solely or in partnership) in Eire, an additional tax of 7s. 6d. in the £ is charged on the excess of either :

(a) Those profits over the statutory standard profits, or

(b) His total income over the statutory total income, whichever is less.

**Exemptions :** (a) Husbandry ; (b) offices and employments ; (c) professions depending on personal qualifications and requiring small capital. Commission businesses are liable.

*Standard Profits.*—£2,500 or the profits of any year out of the last three accounting years ended prior to 6th April, 1930. (If business commenced within the three years one complete year prior to that date.) Otherwise £2,500.

*Standard Income.*—£2,500 or income of one of three years ended before 6th April, 1940.

For further details see Finance Act, 1941, Pt II. and Finance Act, 1942, §§ 1, 4 and 10.

## APPENDIX VII.

## NOTES ON LAND TAX.

Land Tax is assessed and collected with the Schedule A Income Tax, and by the same officers, but for the year ending 24th March. A quota is fixed for each parish. The rates vary from year to year, and between parishes, according to the amount required to raise the quota for the respective parishes, but the rate must not exceed one shilling in the £, nor be less than one penny in the £, unless the lesser rate proposed will entirely extinguish the liability of the parish. The rate for 1940-41 onwards must not exceed that for 1939-40 (§ 43—1942).

If a parish raises more than its quota in any year, subsequent quotas are reduced by ten per cent. of the excess. The tax is charged either on rateable value or the gross Schedule A value. The tax is a landlord's burden, but is normally collected from the occupier, who can deduct it from the rent. Individual owners (not companies, etc.) are exempt if their incomes do not exceed £160, and are liable at half rate if the incomes are over £160, but not over £400 (§ 12—1898, § 63—1920). If the relief was not claimed before the tax was paid, repayment may be obtained on a claim within one year of the end of the land tax year (§ 52—1938). The income to be taken is that to 5th April in the land tax year (§ 54—1927).

The due date is 1st January in the year of assessment. Appeals must be made within twenty-one days of the notice of assessment, or if none is received, within twelve months of the end of the year of assessment, and are heard by the Land Tax Commissioners. Appeal does not stop collection, but any tax overpaid will be repaid (§ 42 and 10th Sch., Pt. II—1942).

Land Tax can be redeemed at any time on payment of an amount equal to twenty-five times the tax payable for 1939-40 (§§ 32 and 33—1896; § 64—1921; § 43—1942). This provision is obviously of importance where land is to be built on, and the tax should be redeemed before the land rises in value and the assessments are consequently increased.

## APPENDIX VIII.

## NOTES ON CORPORATION DUTY.

Corporation Duty was imposed by § 11 (1), Customs and Inland Revenue Act, 1885, owing to the fact that certain property, by reason of its belonging to or being vested in bodies corporate or unincorporate, escapes liability to death duties, and it is expedient to impose a duty thereon by way of compensation to the revenue. The duty is levied in respect of all real and personal property which shall have belonged to or been vested in any body corporate or unincorporate during the yearly period ending on 5th April in any year, and is at the rate of £5 per cent. upon the annual value, income, or profits of such property accrued to such body corporate or unincorporate in the same fiscal year, after deducting therefrom all necessary outgoings, including the receiver's remuneration, and costs, charges, and expenses properly incurred in the management of such property.

The following property is exempt :—

- (1) Property vested in or under the control or management of the Commissioners of Works or any Department of Government.
- (2) Property which, or the income or profits whereof, shall be legally appropriated and applied for the benefit of the public at large or of any county, shire, borough, or place, or the ratepayers or inhabitants thereof, or in any manner expressly prescribed by Act of Parliament.
- (3) Property which, or the income or profits whereof, shall be legally appropriated and applied for any purpose connected with any religious persuasion, or for any charitable purpose, or for the promotion of education, literature, science, or the fine arts.
- (4) Property of any friendly society or savings bank established according to Act of Parliament. (This does not exempt workmen's clubs.)
- (5) Property belonging to or constituting the capital of a body corporate or unincorporate established for any trade or business, or being the property of a body whose capital stock is so divided and held as to be liable to be charged to legacy duty or succession duty. (This exempts most limited companies.)
- (6) Property acquired by or with funds voluntarily contributed to any body corporate or unincorporate within a period of thirty years immediately preceding the year of assessment. (Members subscriptions and other payments made in accordance with the rules of the body are not deemed to be "funds voluntarily subscribed.")
- (7) Property acquired by any body corporate or unincorporate within a period of thirty years immediately preceding where legacy duty or succession duty shall have been paid upon the acquisition thereof (*ibid.* § 11).

The term "body unincorporate" includes every unincorporated company, fellowship, society, association, and trustee, or number of trustees, to or in whom respectively any real or personal property shall belong in such manner, or be vested upon such permanent trusts, that the same shall not be liable to legacy duty or succession duty.

The term "accountable officer" means every chamberlain, treasurer, bursar, receiver, secretary, or other officer, trustee, or member of a body corporate or unincorporate by whom the annual income or profits of property, in respect whereof duty is chargeable under this Act shall be received, or in whose possession, or under whose control, the same shall be (*ibid.* § 12).

The duty is considered as a stamp duty, and is under the care and management of the Commissioners of Inland Revenue, who have the same powers and authorities for the collection, recovery, and management thereof as are vested in them for the collection, recovery and management of Succession Duty (§ 13).

The duty is a first charge on all the property in respect of which it is payable while such property remains in the possession or under the control of the body corporate or unincorporate chargeable with such duty, or of any party or parties acquiring the same, with notice of any such duty being in arrear, and every such body corporate or unincorporate and every accountable officer, is, to the full extent of the property, answerable for the payment of the duty charged on it (§ 14).

Every body corporate or unincorporate chargeable with the duty must on or before 1st October in every year, deliver, or cause to be delivered, to the Commissioners or their officers, a full and true account of all property in respect of which the duty is payable, and of the gross annual value, income, or profits thereof accrued to the same body in the year ended on the preceding fifth day of April, and of all deductions claimed in respect thereof, whether by relation to any of the before-mentioned exemptions from such duty or as necessary outgoings.

The account must be made in the form presented by the Commissioners and every accountable officer liable for payment of duty in respect of any property chargeable is answerable also for the delivery to the Commissioners of the return relating to such property (§ 15).

Every accountable officer is authorised to retain or raise out of any moneys of any body corporate or unincorporate which shall be held by him, or shall come to his hands, the full amount of all moneys which he shall pay or have paid on account of the duty, and all reasonable expenses incident to such payments (§ 16).

The Commissioners may assess the duty upon the footing of any account rendered to them, or if dissatisfied with such account may cause an account to be taken by any person or persons appointed by themselves for that purpose, and assess the duty on the footing of such account subject to appeal to a court in the same manner as in any case of Succession Duty.

If the duty so assessed exceeds the duty assessable according to the account rendered to the Commissioners, and with which they shall have been dissatisfied, and if there is no appeal against such assessment, then it is in the discretion of the Commissioners, having regard to the merits of each case, to charge the whole or any part of the expenses incident to the taking of the special account on any funds liable to duty as an addition to and part of such duty and to recover it accordingly; but if there is an appeal against the assessment, then the payment of the expenses is in the discretion of the court.

The duty is payable immediately after the assessment and notwithstanding any appeal therefrom; but in the event of the amount of the assessment being reduced by the order of the court, the difference in amount shall be repaid with such interest (if any) as the court may allow (§ 17).

Every body corporate or unincorporate, and every accountable officer required to deliver any account and wilfully neglecting so to do on or before 1st October in any year is liable to 10 per cent. on the amount of duty payable in respect of the property required to be comprised in such account, and a like penalty for every month after the first month during which such neglect continues.

Every body corporate or unincorporate, and every accountable officer required to pay any duty, and wilfully neglecting to do so for a space of twenty-one days after it becomes payable, is liable to a penalty equal to ten per cent. on the amount of the unpaid duty, and a like penalty for every month after the expiration of the said period of twenty-one days during which such neglect continues (§ 18).

The Commissioners have the same powers in relation to proceedings to enforce the delivery of accounts, and in relation to the verification of accounts, and the production and inspection of books and documents, as they have in relation to Succession Duty.

Every body corporate or unincorporate, dissatisfied with the assessment of the Commissioners, may appeal in the same manner to the same courts, and subject to the same provisions in, to, and subject to which any accountable party may appeal in relation to Succession Duty (§ 19).

In the case of any proceeding in any court for the administration of any property chargeable with duty the court must provide out of any such property in its possession or control for the payment of the duty to the Commissioners (§ 20).

#### Returns.

Forms are issued by the Secretary to the Board of Inland Revenue, Assessments Division, requiring the following information :—

- (1) Situation and description of real and leasehold property, the name of the occupier and the gross annual value for Income Tax purposes, if occupied by the owner, or the gross rental, if let.
- (2) Particulars of fines, royalties, etc.
- (3) Description of stocks in public funds, showing the period for which held in the year and the rate of interest received, the names in which invested or deposited, the nominal amount held, and gross income therefrom.
- (4) Similar particulars in respect of the personal property, including securities for money and deposits in bank.

#### Assessment.

The liability is based on the actual gross income of the year of assessment, ended 5th April, but the accounts ended in the year are accepted. A copy of the accounts should accompany the Return.

*Deductions* are allowed for the following :—

- (1) Ground rent (gross) and mortgage and debenture interest (gross).
- (2) Insurance for the structure of the property, excluding contents.
- (3) Necessary repairs to property charged, excluding improvements and repairs to equipment.
- (4) Expenses incidental to the management of the property and to the realisation of the income.
- (5) The salary of the receiver, or a fair proportion thereof.
- (6) Income legally appropriated to charitable purposes and funds from property exempted as already stated in (6) and (7) above.

#### Computation.

The Computation is as follows :—

##### Annual Value, Income or Profits of Real and Leasehold Property—

Property in occupation of owner	..	..	£
Property let	..	..	£
<hr/>			
Total	..	..	£
Annual Income of Personal (other than	..	..	
Leasehold) Property	..	..	£
<hr/>			
Total Property	..	..	£
Total Amount of Deductions Claimed	..	..	£
<hr/>			
Net Annual Value, Income or Profits	..	..	£
<hr/>			

The duty of 5% is computed on the Net total.

**Illustration—**

A professional body was incorporated under the Companies Act with permission to dispense with the word "limited" as part of its name. The Income and Expenditure Account for the year ended 31st March, 1948, was as follows:—

<i>Dr.</i>			<i>Cr.</i>		
	£			£	
To Salaries .. ..	1,500		By Subscriptions ..	2,900	
„ General Expenses ..	3,000		„ Interest on Investments		
„ Insurance—			less tax .. ..	1,760	
Buildings owned £12			„ Rents Received, less		
„ let 58			tax .. ..	860	
Contents .. 20			„ Excess of Expenditure		
	90		over Income ..	25	
„ Ground Rent, less tax	22				
„ Mortgage Interest, less					
tax .. ..	660				
„ Schedule A tax ..	216				
„ Agent's Commission ..	57				
	<u>£5,545</u>			<u>£5,545</u>	

The Net Annual Value of the property let is £1,200.

Compute the Corporation Duty payable for 1947-48 assuming that General Expenses include £115 repairs to the structure of buildings, and that it is agreed to allow the proportion of the salaries and general expenses that the income liable bears to total income.

	£	
Gross Annual Value of property in occupation of owner ..	580	
Gross Rents received from property let .. ..	1,400	
	<u>1,980</u>	
Annual Income of Personal Property—		
Gross Interest received .. .. .	3,200	
	<u>5,180</u>	
Deductions claimed—		
Ground Rent .. .. .	£40	
Mortgage Interest .. .. .	1,200	
Repairs .. .. .	115	
Insurance .. .. .	70	
Agent's Commission .. .. .	57	
	<u>5,180</u>	
General Expenses .. .. .		
of £ (1,500 + 3,000 - 115)	2,811	
	<u>4,293</u>	
Net Income liable .. .. .	<u>£887</u>	
Duty thereon at 5% =	<u>£44 7s. 0d.</u>	

NOTES.—(1) Since the Schedule A tax paid amounts to £216, i.e., tax at 9s. 0d. on £480, the gross annual value of the property owned is £100 + £ (480 — £80) = £580.

(2) Since the net annual value of the property let is £1,200, the tax thereon at 9s. 0d. is £540, the amount deducted from the rent. Hence the gross rent is £860 + £540 = £1,400.

## APPENDIX IX.

### MINERAL RIGHTS DUTY.

This duty was imposed by the Finance (1909-10) Act, 1910, § 20, on the rental value of all rights to work minerals and of all mineral wayleaves. It includes the right to work brine or sand, chalk, limestone or gravel but not common clay, common brick clay or common brick earth (*Attorney-General v. Salt Union* (1917), 2 K.B. 488).

The duty is 1/- in the £ of rental value.

#### *Rental Value:—*

- |                               |  |
|-------------------------------|--|
| (a) Minerals leased—          | the rent paid in the preceding year.                                       |
| (b) Minerals worked by owner— | amount fixed by the Commissioners of Inland Revenue as equivalent to rent. |
| (c) Mineral wayleaves—        | the rent paid in the preceding year  |

Where the rent is more than that customary in the district, and represents a return for expenditure by the owner of sums borne normally by the lessee, a reduction in the assessment can be claimed.

#### *Returns.*

Must be made within 30 days of receipt of notice from the Inland Revenue.

#### *Assessment.*

On rent received, i.e., less Income Tax (but not Sur-tax). The working year ends on 30th September, and the duty is payable on or after 1st January thereafter. See Chap. IX, § 8 as to claim for costs of management for Income Tax purposes.

### ROYALTIES WELFARE DUTY.

This duty was imposed by the Mining Industry Act, 1926, for the benefit of the Miners' Welfare Fund. Every person liable to pay Mineral Rights Duty on the rental value of rights to work coal and of mineral wayleaves in connection with coal is liable to pay 1/- in the £ on the rental value. The duty is collected with the Mineral Rights Duty, and is assessed under the same rules.

## APPENDIX X.

## TRANSFER OF ASSETS ABROAD.

SECTION 18, FINANCE ACT, 1936,\*

AS AMENDED BY SECTION 28, FINANCE ACT, 1938.

(The provisions in italics preceded by an asterisk were incorporated by § 28, 1938, and apply for Income Tax 1938-39 onwards, and for Sur-tax 1937-38 onwards.)

For the purpose of preventing the avoiding by individuals ordinarily resident in the United Kingdom of liability to Income Tax by means of transfers of assets by virtue or in consequence whereof, either alone or in conjunction with associated operations, income becomes payable to persons resident or domiciled out of the United Kingdom, it is hereby enacted as follows:—

- (1) Where such an individual has by means of any such transfer, either alone or in conjunction with associated operations, acquired any rights by virtue of which he has, within the meaning of this section, power to enjoy, whether forthwith or in the future, any income of a person resident or domiciled out of the United Kingdom which, if it were income of that individual received by him in the United Kingdom, would be chargeable to Income Tax by deduction or otherwise, that income shall, whether it would or would not have been chargeable to Income Tax apart from the provisions of this section, be deemed to be income of that individual for all the purposes of the Income Tax Acts:

*\*(1A). Where, whether before or after any such transfer, such an individual receives or is entitled to receive any capital sum the payment whereof is in any way connected with the transfer and any associated operations, any income which, by virtue or in consequence of the transfer either alone or in conjunction with associated operations, has become the income of a person, resident or domiciled out of the United Kingdom shall, whether it would or would not have been chargeable to income tax apart from the provisions of this section, be deemed to be the income of that individual for all the purposes of the Income Tax Acts.*

*In this section the expression "capital sum" means—*

*(a) any sum paid or payable by way of loan or repayment of a loan; and*

*(b) any other sum paid or payable otherwise than as income, being a sum which is not paid or payable for full consideration in money or money's worth.*

*\*(1B). The last two foregoing subsections shall not apply if the individual shows in writing or otherwise to the satisfaction of the Special Commissioners either—*

*(a) that the purpose of avoiding liability to taxation was not the purpose or one of the purposes for which the transfer or associated operations or any of them were effected; or*

*(b) that the transfer and any associated operations were bona fide commercial transactions and were not designed for the purpose of avoiding liability to taxation.*

*\*Added by § 28 (2)—1938.*



- (2) For the purposes of this section an associated operation means, in relation to any transfer, an operation of any kind effected by any person, in relation to any of the assets transferred or any assets representing, whether directly or indirectly, any of the assets transferred, or to the income arising from any such assets, or to any assets representing, whether directly or indirectly, the accumulations of income arising from any such assets.
- (3) An individual shall, for the purposes of this section, be deemed to have power to enjoy income of a person resident or domiciled out of the United Kingdom if—
- (a) the income is in fact so dealt with by any person as to be calculated, at some point of time, and whether in the form of income or not, to inure for the benefit of the individual; or
  - (b) the receipt or accrual of the income operates to increase the value to the individual of any assets held by him or for his benefit; or
  - (c) the individual receives or is entitled to receive, at any time, any benefit provided or to be provided out of that income or out of moneys which are or will be available for the purpose by reason of the effect or successive effects of the associated operations on that income and on any assets which directly or indirectly represent that income; or
  - (d) the individual has power, by means of the exercise of any power of appointment or power of revocation or otherwise, to obtain for himself, whether with or without the consent of any other person, the beneficial enjoyment of the income, *\*or may, in the event of the exercise of any power vested in any other person, become entitled to the beneficial enjoyment of the income; or*
- \* Added by § 28 (3)—1938.*
- (e) the individual is able in any manner whatsoever, and whether directly or indirectly, to control the application of the income.
- (4) In determining whether an individual has power to enjoy income within the meaning of this section, regard shall be had to the substantial result and effect of the transfer and any associated operations, and all benefits which may at any time accrue to the individual as a result of the transfer, and any associated operations shall be taken into account irrespective of the nature or form of the benefits.

*\*(4A). For the purpose of this section any body corporate incorporated outside the United Kingdom shall be treated as if it were resident out of the United Kingdom whether it is so resident or not.*

*\* Added by § 28 (4)—1938.*

- (5) For the purposes of this section—
- (a) a reference to an individual shall be deemed to include the wife or husband of the individual;
  - (b) the expression "assets" includes property or rights of any kind, and the expression "transfer," in relation to rights includes the creation of those rights;
  - (c) the expression "benefit" includes a payment of any kind;
  - (d) references to income of a person resident or domiciled out of the United Kingdom shall, where the amount of the income of a company for any year or period has been apportioned under Section 21 of the Finance Act, 1922, include references to so much of the income of the company for that year or period as is equal to the amount so apportioned to that person;

(e) references to assets representing any assets, income or accumulations of income include references to shares in or obligations of any company to which, or obligations of any other person to whom, those assets, that income or those accumulations are or have been transferred.

- (6) The provisions of the Second Schedule to this Act shall have effect for the purpose of carrying this section into effect and otherwise for supplementing the provisions of this section, and this section is referred to in that Schedule as "the principal section."
- (7) The provisions of this section shall apply for the purposes of assessment to Income Tax for the year 1935-36 and subsequent years, and shall apply in relation to transfers of assets and associated operations whether carried out before or after the commencement of this Act :

Provided that, for the year 1935-36, no income shall be charged to tax at the standard rate by virtue of the provisions of this section, but Sur-tax shall be assessed and charged as if any income which would, but for this proviso, have been charged as aforesaid had in fact been so charged.

The Second Schedule referred to is as follows :—

*Supplementary Provisions as to Prevention of Avoidance of Income Tax by Transactions resulting in the Transfer of Income to Persons Abroad.*

- (1) Tax at the standard rate shall not be charged by virtue of the principal section in respect of income which has borne tax at the standard rate by deduction or otherwise but, save as aforesaid, tax chargeable at the standard rate by virtue of that section shall be charged under Case VI of Schedule D, and all assessments in respect thereof shall be made by the Special Commissioners.
- (2) In computing the liability to Income Tax of an individual chargeable by virtue of the provisions of the principal section the same deductions and reliefs shall be allowed as would have been allowed if the income deemed to be his by virtue of that section had actually been received by him.
- (3) Where an individual has been charged to Income Tax on any income deemed to be his by virtue of the principal section and that income is subsequently received by him, it shall be deemed not to form part of his income again for the purposes of the Income Tax Acts.
- (4) All the provisions of the Income Tax Acts relating to the charge, assessment, collection and recovery of Income Tax, to appeals against assessments made by the Special Commissioners and to cases to be stated for the opinion of the High Court shall apply to any Income Tax chargeable by virtue of the principal section, so far as they are applicable and subject to any necessary modifications.
- (5) For the purposes of an assessment under the principal section the Special Commissioners shall have any of the powers of a surveyor, and for the purpose of the representation of the Crown before the Special Commissioners on any appeal under this Schedule, any person nominated in that behalf by the Commissioners of Inland Revenue shall have all such powers as a surveyor has at and upon, the determination of an appeal.

- (6) The Special Commissioners may by notice in writing require any person to furnish them within such time as they may direct (not being less than twenty-eight days) with such particulars as they think necessary for the purpose of the principal section, and if that person, without reasonable excuse, fails to comply with the notice he shall be liable to a penalty not exceeding fifty pounds, and after judgment has been given for that penalty, to a further penalty of the like amount for every day during which the failure continues.
- (7) Without prejudice to the provisions of the last foregoing paragraphs, if any individual fails to furnish any particulars required under this Schedule, or if the Special Commissioners are not satisfied with any particulars furnished under this Schedule, they may make an estimate of the amount of the income which, by virtue of the provisions of the principal section, is to be deemed to be the income of the individual for the purposes of the Income Tax Acts.

By section 17, 1939—

- (1) It is hereby declared that the particulars which a person must furnish to the Special Commissioners under paragraph 6 of the Second Schedule to the Finance Act, 1938 (which Schedule contains supplementary provisions as to the prevention of avoidance of Income Tax by transactions resulting in the transfer of income to persons abroad), if he is required by a notice from those Commissioners so to do, include particulars—

(a) as to transactions with respect to which he is or was acting on behalf of others ;

(b) as to transactions which in the opinion of the Commissioners it is proper that they should investigate for the purposes of section eighteen of the Finance Act, 1938, notwithstanding that in the opinion of the person to whom the notice is given no liability to tax arises under the said section ;

(c) as to whether the person to whom the notice is given has taken or is taking any, and, if so what, part in any, and if so what, transactions of a description specified in the notice.

- (2) Notwithstanding anything in subsection (1) of this section a solicitor shall not be deemed for the purposes of paragraph (c) thereof to have taken part in a transaction by reason only that he has given professional advice to a client in connection with that transaction, and shall not in relation to anything done by him on behalf of a client, be compellable under the said paragraph 6, except with the consent of his client, to do more than state that he is or was acting on behalf of a client and give the name and address of his client and also,

(a) in the case of anything done by the solicitor in connection with the transfer of any asset by or to an individual ordinarily resident in the United Kingdom to or by any such body corporate as is hereinafter mentioned, or in connection with any associated operation in relation to any such transfer, the names and addresses of the transferor and the transferee, or of the persons concerned in the associated operations as the case may be ;

(b) in the case of anything done by the solicitor in connection with the formation or management of any such body corporate as is hereinafter mentioned, the name and address of the body corporate ;

(c) in the case of anything done by the solicitor in connection with the creation, or with the execution of the trusts, of any settlement by virtue or in consequence whereof income becomes payable to a person resident or domiciled out of the United Kingdom, the names and addresses of the settlor and of that person.

The bodies corporate mentioned in the preceding provisions of this subsection are bodies corporate resident or incorporated outside the United Kingdom which are, or, if they were incorporated in the United Kingdom, would be investment companies to which section twenty-one of the Finance Act, 1922, applies.

- (3) Nothing in this section shall impose on any bank the obligation to furnish any particulars of any ordinary banking transactions between the bank and a customer carried out in the ordinary course of banking business, unless the bank has acted or is acting on behalf of the customer in connection with the formation or management of any such body corporate as is mentioned in paragraph (b) of subsection (2) of this section or in connection with the creation, or with the execution of the trusts, of any such settlement as is mentioned in paragraph (c) thereof.

- (4) For the purposes of this section—

(a) the expression "settlement" and "settlor" have the meanings assigned to them respectively by paragraph (b) of subsection (4) of section forty-one of the Finance Act, 1938;

(b) the expression "investment company" has the same meaning as in section twenty of the Finance Act, 1936.

## APPENDIX XI.

## SETTLEMENTS.

## FINANCE ACT, 1922, SECTION 20.

The following are the relevant provisions:—

## 20.—(1) ANY INCOME—

(a) \* [OF WHICH ANY PERSON IS ABLE, OR HAS, AT ANY TIME SINCE THE FIFTH DAY OF APRIL, NINETEEN HUNDRED AND TWENTY-TWO, BEEN ABLE, WITHOUT THE CONSENT OF ANY OTHER PERSON BY MEANS OF THE EXERCISE OF ANY POWER OF APPOINTMENT, POWER OF REVOCATION OR OTHERWISE HOWSOEVER BY VIRTUE OR IN CONSEQUENCE OF A DISPOSITION MADE DIRECTLY OR INDIRECTLY BY HIMSELF, TO OBTAIN FOR HIMSELF THE BENEFICIAL ENJOYMENT; OR]

(b) † which by virtue or in consequence of any disposition made, directly or indirectly, by any person after the first day of May, nineteen hundred and twenty-two (other than a disposition made for valuable and sufficient consideration), IS PAYABLE TO OR APPLICABLE FOR THE BENEFIT OF ANY OTHER PERSON FOR A PERIOD WHICH CANNOT EXCEED SIX YEARS;

(c) ‡ Which by virtue or in consequence of any disposition made, directly or indirectly, by any person after the fifth day of April, nineteen hundred and fourteen, is payable to or applicable for the benefit of a child of that person for some period less than the life of the child,

shall, subject to the provisions of this section, but in cases under the above paragraph (c) only if and so long as the child is an infant and unmarried, be deemed for the purposes of the enactments relating to Income Tax (including Sur-tax) to be the income of the person who is or was able to obtain the beneficial enjoyment thereof, or of the person, if living, by whom the disposition was made, as the case may be, and not to be for those purposes the income of any other person:

\* [Provided that in cases under the above paragraph (a)—

(i) where any such power as aforesaid can be exercised by a person with the consent of the wife or the husband of that person, the power shall for the purposes of the said paragraph, be deemed to be exercisable without the consent of another person, except where the husband and wife are living apart either by agreement or under an order of a court of competent jurisdiction; and

(ii) where any such power as aforesaid is exercisable by the wife or the husband of the person who made the disposition, the power shall, for the purposes of the said paragraph, be deemed to be exercisable by the person who made the disposition.]

Provided [also] that—

(i) the above paragraph (c) shall not apply as regards any income which is derived from capital which, at the end of the period during which that income is payable to or applicable for the benefit of the child, is required by the disposition to be held on trust absolutely for, or to be transferred to, the child, or any income which is payable to or applicable for the benefit of a child during the whole period of the life of the person by whom the disposition was made; and

\* [ ] repealed by § 55, 5th Sch., 1938, with effect from 1937-38 as regards Sur-tax. See § 11 (2) and 3rd Sch., Part II, para. 5, as to savings in certain cases.

† See 3rd Sch., Part II, 1938, as to certain new settlements.

‡ Ceases to have effect in certain cases. See § 21, 1936.

\*\* [ ] repealed by § 55 (7) and 5th Sch., 1938.

(ii) for the purposes of the said paragraph (c) income shall not be deemed to be payable to or applicable for the benefit of a child for some period less than its life by reason only that the disposition contains a provision for the payment to some other person of the income in the event of the bankruptcy of the child, or of an assignment thereof, or a charge thereon being executed by the child.

(2) Where by virtue of paragraph (b) or paragraph (c) of subsection (1) of this section any Income Tax or Sur-tax becomes chargeable on and is paid by the person by whom the disposition was made, that person shall be entitled to recover from any trustee or other person to whom the income is payable by virtue or in consequence of the disposition the amount of the tax so paid, and for that purpose to require the Commissioners concerned to furnish to him a certificate specifying the amount of the income in respect of which he has so paid tax and the amount of the tax so paid, and any certificate so furnished shall be conclusive evidence of the facts appearing thereby. (*See § 21 (5), 1936, as to settlements on children.*)

(3) Where any person obtains in respect of any allowance or relief a repayment of Income Tax in excess of the amount of the repayment to which he would but for the provisions of paragraph (b) or paragraph (c) of subsection (1) of this section have been entitled, an amount equal to the excess shall be paid by him to the trustee or other person to whom the income is payable by virtue or in consequence of the disposition, or where there are two or more such persons shall be apportioned among those persons as the case may require. (*See § 21 (5), 1936, as to settlements on children.*)

If any question arises as to the amount of any payment or as to any apportionment to be made under this subsection, that question shall be decided by the General Commissioners whose decision thereon shall be final.

(4) Any income, which is deemed by virtue of this section to be the income of any person, shall be deemed to be the highest part of this income. (*See § 21 (5), 1936, as to settlements on children.*)

(5) In this section, unless the context otherwise requires—

The expression "disposition" includes any trust, covenant, agreement or arrangement.

The term "any income" which opens Section 20, 1922, must be construed to mean "any income chargeable with tax under the British Finance Act of the year" (*Astor v. Perry* (1935), A.C. 398; 19 T.C. 255).

Section 21, Finance Act, 1936, provides as follows:—

21.—(1) Where, by virtue or in consequence of any settlement to which this section applies and during the life of the settlor, any income is paid to or for the benefit of a child of the settlor in any year of assessment, the income shall, if at the commencement of that year the child was an infant and unmarried, be treated for all the purposes of the Income Tax Acts as the income of the settlor for that year and not as the income of any other person.

(2) Subject as hereafter provided, for the purpose of this section—

(a) income which, by virtue or in consequence of a settlement to which this section applies, is so dealt with that it, or assets representing it, will or may become payable or applicable to or for the benefit of a child of the settlor in the future (whether on the fulfilment of a condition, or the happening of a contingency, or as the result of the exercise of a power or discretion conferred on any person or otherwise) shall be deemed to be paid to or for the benefit of that child; and

(b) any income dealt with as aforesaid which is not required by the settlement to be allocated, at the time when it is so dealt with, to any

particular child or children of the settlor shall be deemed to be paid in equal shares to or for the benefit of each of the children to or for the benefit of whom or any of whom the income or assets representing it will or may become payable or applicable.

(3) Where any income is dealt with as mentioned in the last foregoing subsection by virtue of or in consequence of a settlement to which this section applies, being a settlement which, at the time when the income is so dealt with, is an irrevocable settlement—

- (a) the provisions of the last foregoing subsection shall not apply to that income unless and except to the extent that that income consists of, or represents directly or indirectly, sums paid by the settlor which are allowable as deductions in computing his total income for the purpose of the Income Tax Acts; and
- (b) any sum whatsoever paid thereafter by virtue of or in consequence of the settlement, or any enactment relating thereto, to or for the benefit of a child of the settlor, being a child who at the commencement of the year of assessment in which the sum is paid is an infant and unmarried, shall be deemed for the purposes of subsection (1) of this section to be paid as income, unless and except to the extent that the sum so paid together with any other sums previously so paid (whether to that child or to any other child who, at the commencement of the year of assessment in which that other sum was so paid, was an infant and unmarried) exceeds the aggregate amount of the income which by virtue of or in consequence of the settlement has been paid to or for the benefit of a child of the settlor, or dealt with as mentioned in subsection (2) of this section since the date when the settlement took effect or the date when it became irrevocable, whichever is the later.

(4) Income paid to or for the benefit of a child of a settlor shall not be treated as provided in subsection (1) of this section for any year of assessment in which the aggregate amount of the income paid to or for the benefit of that child, which, but for this subsection, would be so treated by virtue of the foregoing provisions of this section, does not exceed five pounds.

(5) Subsections (2) and (3) of section twenty of the Finance Act, 1922, shall have effect as if references to paragraph (c) of subsection (1) of that section included references to the foregoing provisions of this section, as if references to a disposition included references to a settlement, and as if the reference to the making of a disposition included a reference to the making of or entering into a settlement, and subsection (4) of that section shall have effect as if the reference to that section included a reference to the said provisions of this section.

(6) No repayment shall be made under section twenty-five of the Income Tax Act, 1918, on account of tax paid in respect of any income which by virtue of this section has been treated as the income of a settlor.

(7) The General or Special Commissioners may by notice in writing require any party to a settlement to furnish them within such time as they may direct (not being less than twenty-eight days) with such particulars as they think necessary for the purpose of this section, and if that person without reasonable excuse fails to comply with the notice, he shall be liable to a penalty not exceeding fifty pounds, and, after judgment has been given for that penalty, to a further penalty of the like amount for every day during which the failure continues.

(8) For the purposes of this section, a settlement shall not be deemed to be irrevocable, if the terms thereof provide—

- (a) for the payment to the settlor or during the life of the settlor to the wife or husband of the settlor for his or her benefit, or for the

application for the benefit of the settlor or during the life of the settlor of the wife or husband of the settlor, of any income or assets in any circumstances whatsoever during the life of any child of the settlor to or for the benefit of whom any income, or assets representing it, is or are or may be payable or applicable by virtue or in consequence of the settlement; or

- (b) for the determination of the settlement by the act or on the default of any person; or
- (c) for the payment of any penalty by the settlor in the event of his failing to comply with the provisions of the settlement:

Provided that a settlement shall not be deemed to be revocable by reason only—

- (i) that it contains a provision whereunder any income or assets will or may become payable to or applicable for the benefit of the settlor, or the wife or husband of the settlor, on the bankruptcy of any such child as is mentioned in paragraph (a) of this subsection or in the event of an assignment of or charge on that income or those assets being executed by such a child; or
- (ii) that it provides for the determination of the settlement as aforesaid in such a manner that the determination will not, during the lifetime of any such child as aforesaid, benefit any person other than such a child, or the wife, husband or issue of such a child; or
- (iii) in the case of a settlement to which section thirty-three of the Trustee Act, 1925 [that section provides for the trusts on which property directed to be held on protective trusts shall be held], applies, that it directs income to be held for the benefit of such a child as aforesaid on protective trusts, unless the trust period is a period less than the life of the child or the settlement specifies some event on the happening of which the child would, if the income were payable during the trust period to him absolutely during that period, be deprived of the right to receive the income or part thereof.

(9) In this section—

- (a) the expression "child" includes a stepchild, an adopted child and an illegitimate child;
- (b) the expression "settlement" includes any disposition, trust, covenant, agreement, arrangement or transfer of assets;
- (c) the expression "settlor," in relation to a settlement, includes any person by whom the settlement was made or entered into directly or indirectly, and in particular (but without prejudice to the generality of the foregoing words of this definition) includes any person who has provided or undertaken to provide funds directly or indirectly for the purpose of the settlement, or has made with any other person a reciprocal arrangement for that other person to make or enter into the settlement;
- (d) the expression "income," except in the third and fourth places where it occurs in subsection (1) of this section, includes any income chargeable to Income Tax by deduction or otherwise and any income which would have been so chargeable if it had been received in the United Kingdom by a person resident and ordinarily resident in the United Kingdom, but does not include income arising under a settlement in a year of assessment for which the settlor is not chargeable to Income Tax as a resident in the United Kingdom.

(10) This section applies to every settlement, wheresoever it was made or entered into, and whether it was made or entered into before or after the passing of this Act, except a settlement made or entered into before the twenty-second day of April, nineteen hundred and thirty-six, which immediately before that date was irrevocable.



(11) Paragraph (c) of subsection (1) of section twenty of the Finance Act, 1922, and any other provisions of that subsection relating to that paragraph, shall cease to have effect as respects any settlement to which this section applies.

The provisions of the Finance Act, 1938, are as follows :—

#### PART IV.

#### INCOME TAX (SETTLEMENTS).

*Income arising under certain settlements to be treated as income of settlor.*

38.—(1) If and so long as the terms of any settlement are such that—

- (a) any person has or may have power, whether immediately or in the future, and whether with or without the consent of any other person, to revoke or otherwise determine the settlement or any provision thereof and, in the event of the exercise of the power, the settlor or the wife or husband of the settlor will or may cease to be liable to make any annual payments payable by virtue or in consequence of any provision of the settlement; or
- (b) the settlor or the wife or husband of the settlor may, whether immediately or in the future, cease, on the payment of a penalty, to be liable to make any annual payments payable by virtue or in consequence of any provision of the settlement;

any sums payable by the settlor or the wife or husband of the settlor by virtue or in consequence of that provision of the settlement in any year of assessment shall be treated as the income of the settlor for that year and not as the income of any other person :

Provided that, where any such power as is referred to in paragraph (a) of this subsection cannot be exercised within the period of six years from the time when the first of the annual payments so referred to becomes payable, and the like annual payments are payable in each year throughout that period, the said paragraph (a) shall not apply so long as the said power cannot be exercised.

(2) If and so long as the terms of any settlement are such that—

- (a) any person has or may have power, whether immediately or in the future, and whether with or without the consent of any other person, to revoke or otherwise determine the settlement or any provision thereof; and
- (b) in the event of the exercise of the power, the settlor or the wife or husband of the settlor will or may become beneficially entitled to the whole or any part of the property then comprised in the settlement or of the income arising from the whole or any part of the property so comprised;

any income arising under the settlement from the property comprised in the settlement in any year of assessment or from a corresponding part of that property, or a corresponding part of any such income, as the case may be, shall be treated as the income of the settlor for that year and not as the income of any other person :

Provided that, where any such power as aforesaid cannot be exercised within six years from the time when any particular property first becomes comprised in the settlement, this subsection shall not apply to income arising under the settlement from that property, or from property representing that property, so long as the power cannot be exercised.

(3) If and so long as the settlor has an interest in any income arising under or property comprised in a settlement, any income so arising during the life

of the settlor in any year of assessment shall, to the extent to which it is not distributed, be treated for all the purposes of the Income Tax Acts as the income of the settlor for that year, and not as the income of any other person :

Provided that—

- (a) if and so long as that interest is an interest neither in the whole of the income arising under the settlement nor in the whole of the property comprised in the settlement, the amount of income to be treated as the income of the settlor by virtue of this subsection shall be such part of the income which, but for this proviso, would be so treated as is proportionate to the extent of that interest ; and
- (b) where it is shown that any amount of the income which is not distributed in any year of assessment consists of income which falls to be treated as the income of the settlor for that year by virtue of either of the last two foregoing subsections, that amount shall be deducted from the amount of income which, but for this proviso, would be treated as his for that year by virtue of this subsection.

(4) For the purpose of the last foregoing subsection, the settlor shall be deemed to have an interest in income arising under or property comprised in a settlement, if any income or property which may at any time arise under or be comprised in that settlement is, or will or may become, payable to or applicable for the benefit of the settlor or the wife or husband of the settlor in any circumstances whatsoever :

Provided that the settlor shall not be deemed to have an interest in any income arising under or property comprised in a settlement—

- (a) if and so long as that income or property cannot become payable or applicable as aforesaid except in the event of—
  - (i) the bankruptcy of some person who is or may become beneficially entitled to that income or property ; or
  - (ii) any assignment of or charge on that income or property being made or given by some such person ; or
  - (iii) in the case of a marriage settlement, the death of both the parties to the marriage and of all or any of the children of the marriage ; or
  - (iv) the death under the age of twenty-five or some lower age of some person who would be beneficially entitled to that income or property on attaining that age ; or
- (b) if and so long as some person is alive and under the age of twenty-five during whose life that income or property cannot become payable or applicable as aforesaid except in the event of that person becoming bankrupt or assigning or charging his interest in that income or property.

(5) The provisions of Part I of the Third Schedule to this Act shall have effect as respects the recovery by a settlor of tax with which he becomes chargeable, and the recovery from a settlor of any additional relief to which he becomes entitled, by virtue of this section.

(6) No repayment shall be made under section twenty-five of the Income Tax Act, 1918 (which relates to relief from tax in respect of income accumulated under trusts) on account of tax paid in respect of any income which by virtue of this section has been treated as the income of a settlor.

(7) The foregoing provisions of this section shall apply for the purposes of assessment to Income Tax for the year 1937-38 and subsequent years and shall apply in relation to any settlement, wherever made and whether made before or after the passing of this Act :

Provided that—

- (a) for the year 1937-38 no income shall be charged to tax at the standard rate by virtue of this section, but Sur-tax shall be assessed and charged as if any income which would, but for this proviso, have been charged as aforesaid had in fact been so charged; and
- (b) for the purpose of granting relief from tax at the standard rate in respect of any income which for the year 1937-38 is treated as the income of a settlor by virtue of subsection (1) or subsection (2) of this section but would be treated as the income of some other person but for that subsection, that income shall be treated as the income of that other person; and
- (c) the provisions of this subsection shall have effect, in relation to a settlement made before the twenty-seventh day of April nineteen hundred and thirty-eight, subject to the provisions of Part II of the Third Schedule to this Act, and in that Part of that Schedule this section is referred to as "the relative section."

*Disallowance of deduction from total income of certain sums paid by settlor.*

39.—(1) Where, by virtue or in consequence of any settlement to which this section applies, the settlor pays directly or indirectly in any year of assessment to the trustees of the settlement any sums which would, but for this subsection, be allowable as deductions in computing his total income for that year for the purposes of Sur-tax, those sums shall not be so allowable to the extent to which the aggregate amount thereof falls within the amount of income arising under the settlement in that year which has not been distributed, less—

- (a) so much of any income arising under the settlement in that year which has not been distributed as is shown to consist of income which has been treated as the income of the settlor by virtue of subsection (1) or subsection (2) of the last foregoing section; and
- (b) the amount of income so arising in that year which is treated as the income of the settlor by virtue of subsection (3) of the last foregoing section.

(2) For the purpose of the last foregoing subsection, any sum paid in any year of assessment by the settlor to any body corporate connected with the settlement in that year shall be treated as if it had been paid to the trustees of the settlement in that year by virtue or in consequence of the settlement.

(3) No relief shall be given under any of the provisions of the Income Tax Acts on account of tax paid in respect of so much of any income arising under a settlement in any year of assessment as is equal to the aggregate amount of any sums paid by the settlor in that year, which are not allowable as deductions by virtue of this section.

(4) This section shall apply to any settlement (wherever made) made after the twenty-sixth day of April nineteen hundred and thirty-eight, and where income arising under any settlement (wherever made) made on or before that date is treated as the income of the settlor by virtue of subsection (1) or subsection (2) of the last foregoing section but ceases to be so treated by reason of any variation of the terms of the settlement made after that date, or would have been so treated but for such a variation, this section shall apply to that settlement as from the date when the variation takes effect.

(5) In this section references to sums paid by a settlor shall include references to sums paid by the wife or husband of the settlor.

*Sums paid to settlor otherwise than as income.*

40.—(1) Any capital sum paid directly or indirectly in any relevant year of assessment by the trustees of a settlement to which this section applies to the settlor shall—

- (a) to the extent to which the amount of that sum falls within the amount of income available up to the end of that year, be treated for all the purposes of the Income Tax Acts as the income of the settlor for that year ;
- (b) to the extent to which the amount of that sum exceeds the amount of income available up to the end of that year but falls within the amount of the income available up to the end of the next following year, be treated for the purposes aforesaid as the income of the settlor for the next following year ;

and so on.

(2) For the purpose of the last foregoing subsection, the amount of income available up to the end of any year shall, in relation to any capital sum paid as aforesaid, be taken to be the aggregate amount of income arising under the settlement in that year and any previous relevant year which has not been distributed, less—

- (a) the amount of any other capital sums paid to the settlor in any relevant year before that sum was paid ; and
- (b) so much of any income arising under the settlement in that year and any previous relevant year which has not been distributed as is shown to consist of income which has been treated as income of the settlor by virtue of subsection (1) or subsection (2) of section thirty-eight of this Act ; and
- (c) any income arising under the settlement in that year and any previous relevant year which has been treated as the income of the settlor by virtue of subsection (3) of section thirty-eight of this Act ; and
- (d) any sums paid by virtue or in consequence of the settlement, to the extent that they are not allowable, by virtue of the last foregoing section, as deductions in computing the settlor's income for that year or any previous relevant year ; and
- (e) an amount equal to tax at the standard rate on
  - (i) the aggregate amount of income arising under the settlement in that year and any previous relevant year which has not been distributed, less
  - (ii) the aggregate amount of the income and sums referred to in paragraphs (b), (c) and (d) of this subsection.

(3) For the purpose of this section, any capital sum paid to the settlor in any year of assessment by any body corporate connected with the settlement in that year shall be treated as having been paid by the trustees of the settlement in that year.

(4) Where the whole or any part of any sum is treated by virtue of this section as income of the settlor for any year, it shall be treated as income of such an amount as, after deduction of tax at the standard rate for that year, would be equal to that sum or that part thereof.

(5) This section applies to any settlement wherever made and whether made before or after the commencement of this Act, and in this section—

- (a) the expression " capital sum " means—
  - (i) any sum paid by way of loan or repayment of a loan ; and
  - (ii) any other sum paid otherwise than as income, being a sum which is not paid for full consideration in money or money's worth ;

but does not include any sum which could not have become payable to the settlor except in one of the events specified in the proviso to subsection (4) of section thirty-eight of this Act ;

- (b) the expression "relevant year" means any year of assessment after the year 1937-38 ;
- (c) references to sums paid to the settlor include references to sums paid to the wife or husband of the settlor.

*Supplementary provisions as to settlements.*

41.—(1) The provisions of Part III of the Third Schedule to this Act shall have effect for the purpose of carrying this Part of this Act into effect and otherwise for supplementing the provisions thereof.

(2) Paragraph (a) of subsection (1) of section twenty of the Finance Act, 1922, shall cease to have effect, and shall be deemed to have ceased to have effect for the purpose of assessment to Sur-tax for the year 1937-38.

(3) Subject to the last foregoing subsection, the provisions of this Part of this Act shall be in addition to and not in derogation of any other provisions of the Income Tax Acts.

(4) For the purposes of this Part of this Act—

(a) the expression "income arising under a settlement" includes—

(i) any income chargeable to Income Tax by deduction or otherwise, and any income which would have been so chargeable if it had been received in the United Kingdom by a person domiciled, resident and ordinarily resident in the United Kingdom ; and

(ii) where the amount of the income of any body corporate has been apportioned under section twenty-one of the Finance Act, 1922, for any year or period, or could have been so apportioned if the body corporate were incorporated in any part of the United Kingdom, so much of the income of the body corporate for that year or period as is equal to the amount which has been or could have been so apportioned to the trustees of or a beneficiary under the settlement ;

but, where the settlor is not domiciled, or not resident, or not ordinarily resident, in the United Kingdom in any year of assessment, does not include income arising under the settlement in that year in respect of which the settlor, if he were actually entitled thereto, would not be chargeable to Income Tax by deduction or otherwise by reason of his not being so domiciled, resident or ordinarily resident ;

(b) the expression "settlement" includes any disposition, trust, covenant, agreement or arrangement, and the expression "settlor" in relation to a settlement means any person by whom the settlement was made ;

(c) a person shall be deemed to have made a settlement if he has made or entered into the settlement directly or indirectly, and in particular (but without prejudice to the generality of the foregoing words of this paragraph) if he has provided or undertaken to provide funds directly or indirectly for the purpose of the settlement, or has made with any other person a reciprocal arrangement for that other person to make or enter into the settlement ;

(d) income arising under a settlement in any year of assessment shall be deemed not to have been distributed if and to the extent that it exceeds the aggregate amount of—

(i) the sums paid in that year by the trustees of the settlement to any persons (not being a body corporate connected with the

settlement and not being the trustees of another settlement made by the settlor or the trustees of the settlement) in such manner that they fall to be treated in that year, otherwise than by virtue of the last preceding section, as the income of those persons for the purposes of Income Tax, or would fall to be so treated if those persons were domiciled, resident and ordinarily resident in the United Kingdom and the sums had been paid to them therein; and

(ii) any expenses of the trustees of the settlement paid in that year which, in the absence of any express provision of the settlement, would be properly chargeable to income, in so far as such expenses are not included in the sums mentioned in the last foregoing sub-paragraph; and

(iii) in a case where the trustees of the settlement are trustees for charitable purposes, the amount by which any income arising under the settlement in that year in respect of which exemption from tax may be granted under section thirty-seven of the Income Tax Act, 1918, or section thirty of the Finance Act, 1921, exceeds the aggregate amount of any such sums or expenses as aforesaid paid in that year which are properly chargeable to that income;

- (e) a body corporate shall be deemed to be connected with a settlement in any year of assessment if any of the income thereof for any year or period ending in that year of assessment--

(i) has been apportioned to the trustees of or a beneficiary under the settlement under section twenty-one of the Finance Act, 1922, or could have been so apportioned if the body corporate had been incorporated in the United Kingdom; or

(ii) could have been so apportioned if the income of the body corporate for that year or period had not been distributed to the members thereof and, in the case of a body corporate incorporated outside the United Kingdom, if the body corporate had been incorporated in the United Kingdom.

### THIRD SCHEDULE.

#### SUPPLEMENTARY PROVISIONS AS TO SETTLEMENTS.

##### PART I.

##### ADJUSTMENTS BETWEEN THE SETTLOR AND TRUSTEES.

1. Where by virtue of any provision of section thirty-eight of this Act any Income Tax becomes chargeable on and is paid by a settlor, he shall be entitled--

- (a) to recover from any trustee, or other person to whom income arises under the settlement, the amount of the tax so paid; and
- (b) for that purpose to require the Commissioners concerned to furnish to him a certificate specifying the amount of income in respect of which he has so paid tax and the amount of tax so paid.

2. Any certificate furnished under the last foregoing paragraph shall be conclusive evidence of the facts stated therein.

3. Where any person obtains, in respect of any allowance or relief, a repayment of Income Tax in excess of the amount of the repayment to which he would, but for the provisions of the said section, have been entitled, an amount equal to the excess shall be paid by him to the trustees or other person to whom income arises under the settlement, or where there are two or more such persons shall be apportioned among those persons, as the case may require.

4. If any question arises as to the amount of any payment or as to any apportionment to be made under the last foregoing paragraph, that question shall be decided by the General Commissioners whose decision thereon shall be final.

5. Any income which is treated by virtue of any provision of the said section as income of a settlor shall be deemed for the purpose of this Schedule to be the highest part of his income.

#### PART II.

##### SPECIAL PROVISIONS AS RESPECTS SETTLEMENTS MADE BEFORE

27TH APRIL, 1938.

1. Subject to the provisions of this Part of this Schedule, in the case of a settlement made before the twenty-seventh day of April nineteen hundred and thirty-eight, subsection (1) of the relative section shall not, by reason only of the provisions of paragraph (a) thereof, apply to sums payable by the settlor by virtue or in consequence of any provision of the settlement in a year to which this Part of this Schedule applies, if—

(a) at the expiration of three months from the date of the passing of this Act—

(i) no person has or can have any such power as is referred to in the said paragraph (a); and

(ii) the settlor has not received and is not entitled to receive any consideration in respect of the release or disclaimer of any such power; or

(b) the like annual payments have been payable by the settlor by virtue or in consequence of that provision of the settlement in each of the seven years of assessment ending with a year to which this Part of this Schedule applies; or

(c) before the expiration of three months from the date of the passing of this Act—

(i) the settlement, or the provision by virtue or in consequence whereof the annual payments are payable, has been revoked; and

(ii) a new settlement has been made by the settlor by virtue or in consequence whereof the settlor is liable to make the like annual payments and cannot, except in the event of his death, cease to be liable to make those payments before the expiration of six years from the date when the first of the annual payments payable by virtue or in consequence of the revoked settlement became payable:

Provided that, where any income arising under the settlement in a year to which this Part of this Schedule applies has not been distributed, the foregoing provisions of this paragraph shall have effect as if there were substituted for the reference to sums payable by the settlor in that year a reference to the amount, if any, by which the sums so payable in that year exceed the income arising under the settlement in that year which has not been distributed.

2. Subject to the provisions of this Part of this Schedule, in the case of a settlement made before the twenty-seventh day of April nineteen hundred and thirty-eight, income arising under the settlement in any year to which this Part of this Schedule applies which would, but for this paragraph, be treated by virtue of subsection (2) of the relative section as the income of the settlor, and not as the income of any other person shall not be so treated or, in a case where any income arising under the settlement in that year has not been distributed, shall not be so treated to the extent that it exceeds the amount of income arising under the settlement in that year which has not

been distributed if, at the expiration of three months from the date of the passing of this Act--

- (a) no person has or can have any such power as is referred to in the said subsection (2); and
- (b) the settlor has not received and is not entitled to receive any consideration in respect of the release or disclaimer of any such power.

3. The foregoing provisions of this Part of this Schedule shall not apply to any settlement if, in any year to which this Part of this Schedule applies, any capital sum within the meaning of section forty of this Act has been paid to the settlor directly or indirectly by the trustees of the settlement or any body corporate connected with the settlement in that year.

4. Notwithstanding that the payments payable by virtue or in consequence of any such new settlement as is referred to in sub-paragraph (c) (ii) of paragraph 1 of this Part of this Schedule are payable to or applicable for the benefit of another person for a period which cannot exceed six years from the date when the settlement was made, they shall not be treated as the income of the settlor by virtue of paragraph (b) of subsection (1) of section twenty of the Finance Act, 1922.

5. Paragraphs 1 and 2 of this Part of this Schedule shall not apply to any income which would have been treated as the income of the settlor for any purpose by virtue of paragraph (a) of subsection (1) of section twenty of the Finance Act, 1922, but for the provisions of this Act relating to that paragraph.

6. In this Part of this Schedule references to the settlor, except where that expression first occurs in paragraph 2, include references to the wife or husband of the settlor.

7. The years to which this Part of this Schedule applies are the year 1937-38 and the year 1938-39.

### PART III.

#### MISCELLANEOUS.

1. Tax chargeable at the standard rate by virtue of sections thirty-eight or forty of this Act shall be charged under Case VI of Schedule D.

2. In computing the liability to Income Tax of a settlor chargeable by virtue of any of the provisions of section thirty-eight of this Act, the same deductions and reliefs shall be allowed as would have been allowed if the income treated as his by virtue of that provision had been received by him.

3. In computing the liability to Income Tax of a settlor chargeable by virtue of section forty of this Act, the same deductions and reliefs shall be allowed as would have been allowed if the amount treated as his income by virtue of that section had been received by him as income.

4. The General or Special Commissioners may by notice in writing require any person, being a party to a settlement, to furnish them (within such time as they may direct, not being less than twenty-eight days) with such particulars as they think necessary for the purposes of any of the provisions of Part IV of this Act, and if that person without reasonable excuse fails to comply with the notice he shall be liable to a penalty not exceeding fifty pounds and, after judgment has been given for that penalty, to a further penalty of the like amount for every day during which the failure continues.

5. Without prejudice to the provisions of the last foregoing paragraph, if any party to a settlement fails to furnish any particulars required under the last foregoing paragraph, or if the General or Special Commissioners are not satisfied with any particulars furnished under that paragraph, they may make an estimate of the amount of income which by virtue of any of the provisions of sections thirty-eight or forty of this Act, is to be treated as the income of the settlor.



(3) In this paragraph—

- (a) references to property or income which a settlor has provided directly or indirectly include references to property or income which has been provided directly or indirectly by another person in pursuance of reciprocal arrangements with that settlor, but do not include references to property or income which that settlor has provided directly or indirectly in pursuance of reciprocal arrangements with another person;
- (b) references to property which represents other property include references to property which represents accumulated income from that other property.

#### PART II.

##### *Application of Finance Act, 1936, § 21.*

1. Subject to the provisions of this Part of this Schedule, section twenty-one of the Finance Act, 1936, has effect in relation to each settlor as if he were the only settlor.

2. For the purposes of the said section twenty-one, only the following can be taken into account, in relation to any settlor, as income paid by virtue or in consequence of the settlement to or for the benefit of a child of the settlor, that is to say,—

- (a) income originating from that settlor; and
- (b) in a case in which paragraph (b) of subsection (3) of the said section twenty-one applies, any sums which are under that paragraph to be deemed to be paid as income:

Provided that in applying the said paragraph (b) to any settlor—

- (i) the references to sums paid by virtue or in consequence of the settlement or any enactment relating thereto include only sums paid out of property originating from that settlor or income originating from that settlor; and
- (ii) the reference to the income which by virtue or in consequence of the settlement has been paid to or for the benefit of a child of the settlor or dealt with as mentioned in subsection (2) of the said section includes only income originating from that settlor.

3. The references in this Part of this Schedule to income originating, and property originating, from a settlor have the meanings assigned to them by paragraph 5 of Part I of this Schedule, except that paragraph (b) of sub-paragraph (2) of the said paragraph 5 must be treated as omitted.

#### PART III.

##### *Application of Finance Act, 1922, § 20.*

1. Subject to the provisions of this Part of this Schedule, section twenty of the Finance Act, 1922, has effect in relation to each person who has made the disposition as if he were the only person who had made it.

2. References in the said section twenty to income payable or applicable by virtue or in consequence of the disposition include, in relation to any person making the disposition, only—

- (a) income from property which that person has provided directly or indirectly for the purposes of the disposition; and
- (b) income from property representing that property; and
- (c) income from so much of any property which represents both property provided as aforesaid and other property as, on a just apportionment, represents the property so provided; and
- (d) income provided directly or indirectly by that person.

3. In this Part of this Schedule, references to property which represents other property include references to property which represents accumulated income from that other property.

Section 28, Finance Act, 1946, provides in regard to Sur-tax on income under settlements :—

(1) Where, during the life of the settlor, income arising under a settlement made on or after the tenth day of April, nineteen hundred and forty-six, is, under the settlement and in the events that occur, payable to or applicable for the benefit of any person other than the settlor, then unless, under the settlement and in the said events, the income either—

- (a) is payable to an individual for his own use ; or
- (b) is applicable for the benefit of an individual named in that behalf in the settlement or of two or more individuals named in that behalf therein ; or
- (c) is applicable for the benefit of a child or children of an individual named in that behalf in the settlement ; or
- (d) is income from property of which the settlor has divested himself absolutely by the settlement ; or
- (e) is income which, by virtue of some provision of the Income Tax Acts other than this section, is to be treated for the purposes of those Acts as income of the settlor,

the income shall be treated for the purposes of Sur-tax as the income of the settlor and not as the income of any other person :

Provided that the exceptions provided for by paragraphs (a), (b) and (c) of this subsection shall not apply where the named individual or individuals or, in the case of the said paragraph (c), either the named individual or the child or any of the children in question, is in the service of the settlor or accustomed to act as the solicitor or agent of the settlor.

(2) The settlor shall not be deemed for the purposes of this section to have divested himself absolutely of any property if that property or any income therefrom or any property directly or indirectly representing proceeds of, or of income from, that property or any income therefrom is, or will or may become, payable to him or applicable for his benefit in any circumstances whatsoever :

Provided that a settlor shall not be deemed not to have divested himself absolutely of any property by reason only that that property or income therefrom or any such other property or income as aforesaid may become payable to him or applicable for his benefit in the event of—

- (a) the bankruptcy of some person who is or may become beneficially entitled to any such property or income ; or
- (b) an assignment of or charge on any such property or income being made or given by some such person ; or
- (c) in the case of a marriage settlement, the death of both the parties to the marriage and of all or any of the children of the marriage ; or
- (d) the death under the age of twenty-five or some lower age of some person who would be beneficially entitled to that property or income on attaining that age.

(3) In this section, the expression “ income arising under a settlement,” “ settlement ” and “ settlor ” have the meanings assigned to them for the purposes of Part IV of the Finance Act, 1938, by sub-section (4) of section forty-one of that Act ; and Part I of the Sixth Schedule to the Finance Act, 1943 (which relates to settlements with more than one settlor), shall have effect in relation to this section as it has effect in relation to the said Part IV.

## APPENDIX XII.

## INCOME FROM RESIDUE.

The following are the relevant provisions of the Finance Act, 1938 :—

## PART III.

## INCOME TAX (ADMINISTRATION OF ESTATES).

*Provisions as to limited interests in residue.*

30.—(1) The following provisions of this section shall have effect in relation to a person who, during the period commencing on the death of a deceased person and ending on the completion of the administration of his estate (in this Part of this Act referred to as "the administration period") or during a part of that period, has a limited interest in the residue of the estate or in a part thereof.

(2) When any sum has been paid during the administration period in respect of that limited interest the amount thereof shall, subject to the provisions of the next following subsection, be deemed for all the purposes of the Income Tax Acts to have been paid to that person as income for the year of assessment in which that sum was paid, or, in the case of a sum paid in respect of an interest that has ceased, for the last year of assessment in which it was subsisting.

(3) On the completion of the administration of the estate—

- (a) the aggregate amount of all sums paid before, or payable on, the completion of the administration in respect of that limited interest shall be deemed to have accrued due to that person from day to day during the administration period or the part thereof during which he had that interest, as the case may be, and to have been paid to him as it accrued due ;
- (b) the amount deemed to have been paid to that person by virtue of the foregoing paragraph in any year of assessment shall be deemed for all the purposes of the Income Tax Acts to have been paid to him as income for that year ; and
- (c) where the amount which is deemed to have been paid to that person as income for any year by virtue of this subsection is less or greater than the amount deemed to have been paid to him as income for that year by virtue of the last foregoing subsection, such adjustments shall be made as are hereafter provided in this Part of this Act.

(4) Any amount which is deemed to have been paid to that person as income for any year by virtue of this section shall—

- (a) in the case of a United Kingdom estate, be deemed to be income of such an amount as would after deduction of standard tax for that year be equal to the amount deemed to have been so paid, and to be income that has borne standard tax ;
- (b) in the case of a foreign estate, be deemed to be income of the amount deemed to have been so paid, and shall be chargeable to standard tax under Case IV of Schedule D as if it were income arising from securities in a place out of the United Kingdom.

(5) Where a person has been charged to standard tax for any year by virtue of this section in respect of an amount deemed to have been paid to him as income in respect of an interest in a foreign estate and any part of the aggregate income of that estate for that year has borne United Kingdom Income Tax by deduction or otherwise, the tax so charged on him shall, on

proof of the facts to the satisfaction of the General or Special Commissioner, be reduced by an amount bearing the same proportion thereto as the amount of the said income which has borne United Kingdom Income Tax, less the tax so borne, bears to the amount of the said aggregate income, less the tax so borne :

Provided that, where relief has been so given, such part of the amount in respect of which he has been charged to standard tax as corresponds to the said proportion shall, for the purposes of Sur-tax, be deemed to represent income of such an amount as would after deduction of standard tax be equal to that part of the amount charged.

*Provisions as to absolute interests in residue.*

31.—(1) The following provisions of this section shall have effect in relation to a person who, during the administration period or during a part of that period, has an absolute interest in the residue of the estate of a deceased person or in a part thereof.

(2) There shall be ascertained in accordance with the next succeeding section the amount of the residuary income of the estate for each whole year of assessment, and for each broken part of a year of assessment, during which—

(a) the administration period was current ; and

(b) that person had that interest ;

and the amount so ascertained in respect of any year or part of a year, or, in the case of a person having an absolute interest in a part of a residue, a proportionate part of that amount, is in this Part of this Act referred to as the " residuary income " of that person for that year of assessment :

Provided that, when the legacy duty charged on the residue, or on the part thereof in which that person has an absolute interest, as the case may be, has been paid in respect of income for any such year or part of a year as aforesaid, his residuary income for that year shall thereafter be treated for the purposes of Sur-tax as reduced by the amount of that duty so far as paid in respect of such income.

(3) When any sum or sums has or have been paid during the administration period in respect of that absolute interest, the amount of that sum or the aggregate amount of those sums shall, subject to the provisions of the next following subsection, be deemed for all the purposes of the Income Tax Acts to have been paid to that person as income to the extent to which, and for the year or years of assessment for which, he would have been treated for those purposes as having received income if he had had a right to receive in each year of assessment—

(a) in the case of a United Kingdom estate, his residuary income for that year less standard tax for that year, or

(b) in the case of a foreign estate, his residuary income for that year, and that sum or the aggregate of those sums had been available for application primarily in or towards satisfaction of those rights as they accrued and had been so applied.

In the case of a United Kingdom estate, any amount which is deemed to have been paid to that person as income for any year by virtue of this subsection shall be deemed to be income of such an amount as would after deduction of standard tax for that year be equal to the amount deemed to have been so paid, and to be income that has borne standard tax.

(4) On the completion of the administration of the estate—

(a) the amount of the residuary income of that person for any year of assessment shall be deemed for all the purposes of the Income Tax Acts to have been paid to him as income for that year, and in the case of a United Kingdom estate shall be deemed to have borne tax by reference to the standard rate ; and

- (b) where the amount which is deemed to have been paid to that person as income for any year by virtue of this subsection is less or greater than the amount deemed to have been paid to him as income for that year by virtue of the last foregoing subsection, such adjustments shall be made as are hereafter provided in this Part of this Act.

(5) In the case of a foreign estate, any amount which is deemed to have been paid to that person as income for any year by virtue of this section shall be deemed to be income of that amount, and shall be chargeable to standard tax under Case IV of Schedule D as if it were income arising from securities in a place out of the United Kingdom.

(6) Where a person has been charged to standard tax for any year by virtue of this section in respect of an amount deemed to have been paid to him as income in respect of an interest in a foreign estate and any part of the aggregate income of that estate for that year has borne United Kingdom Income Tax by deduction or otherwise, the tax so charged on him shall, on proof of the facts to the satisfaction of the General or Special Commissioners, be reduced by an amount bearing the same proportion thereto as the amount of the said income which has borne United Kingdom Income Tax bears to the amount of the said aggregate income.

*Supplementary provisions as to absolute interests in residue.*

32.—(1) The amount of the residuary income of an estate for any year of assessment shall be ascertained by deducting from the aggregate income of the estate for that year—

- (a) the amount of any annual interest, annuity, or other annual payment for that year which is a charge on residue and the amount of any payment made in that year in respect of any such expenses incurred by the personal representatives as such in the management of the assets of the estate as, in the absence of any express provision in a will, would be properly chargeable to income, but excluding any such interest, annuity or payment allowed or allowable in computing the aggregate income of the estate; and
- (b) the amount of any of the aggregate income of the estate for that year to which a person has on or after assent become entitled by virtue of a specific disposition either for a vested interest during the administration period or for a vested or contingent interest on the completion of the administration.

(2) In the event of its appearing, on the completion of the administration of an estate in the residue of which, or in a part of the residue of which, a person had an absolute interest at the completion of the administration, that the aggregate of the benefits received in respect of that interest does not amount to as much as the aggregate for all years of the residuary income of the person having that interest, his residuary income for each year shall be reduced for the purpose of the last foregoing section by an amount bearing the same proportion thereto as the deficiency bears to the aggregate for all years of his residuary income.

In this subsection the expression "benefits received" in respect of an absolute interest means the following amounts in respect of all sums paid before, or payable on, the completion of the administration in respect of that interest, that is to say—

- (a) as regards a sum paid before the completion of the administration, in the case of a United Kingdom estate such an amount as would, after deduction of standard tax for the year of assessment in which that sum was paid, be equal to that sum, or in the case of a foreign estate the amount of that sum; and
- (b) as regards a sum payable on the completion of the administration, in the case of a United Kingdom estate such an amount as would,

after deduction of standard tax for the year of assessment in which the administration is completed, be equal to that sum, or in the case of a foreign estate the amount of that sum.

(3) In the application of the last foregoing subsection to a residue or a part of a residue in which a person other than the person having an absolute interest at the completion of the administration had an absolute interest at any time during the administration period, the aggregates therein mentioned shall be computed in relation to those interests taken together, and the residuary income of that other person also shall be subject to reduction thereunder.

*Special provisions as to certain interests in residue.*

33.—(1) Where the personal representatives of a deceased person have as such a right in relation to the estate of another deceased person such that, if that right were vested in them for their own benefit, they would have an absolute or limited interest in the residue of that estate or in a part thereof, they shall be deemed to have that interest notwithstanding that that right is not vested in them for their own benefit, and any amount deemed to be paid to them as income by virtue of this Part of this Act shall be treated as part of the aggregate income of the estate of the person whose personal representatives they are.

(2) Where different persons have successively during the administration period absolute interests in the residue of the estate of a deceased person or in a part thereof, sums paid during that period in respect of the residue or of that part thereof, as the case may be, shall be treated for the purpose of this Part of this Act as having been paid in respect of the interest of the person who first had an absolute interest therein up to the amount of—

(a) in the case of a United Kingdom estate, the aggregate for all years of that person's residuary income less standard tax, or

(b) in the case of a foreign estate, the aggregate for all years of that person's residuary income,

and, as to any balance up to a corresponding amount, in respect of the interest of the person who next had an absolute interest therein, and so on.

(3) Where upon the exercise of a discretion any of the income of the residue of the estate of a deceased person for any period (being the administration period or a part thereof) would, if the residue had been ascertained at the commencement of that period, be properly payable to any person, or to another in his right, for his benefit, whether directly by the personal representatives or indirectly through a trustee or other person, the amount of any sum paid pursuant to an exercise of the discretion in favour of that person shall be deemed for all the purposes of the Income Tax Acts to have been paid to that person as income for the year of assessment in which it was paid, and the provisions of subsections (4) and (5) of section thirty of this Act shall have effect in relation to an amount which is deemed to have been paid as income by virtue of this subsection.

*Provisions as to adjustments and furnishing of information.*

34.—(1) Where, on the completion of the administration of an estate, any amount is deemed by virtue of this Part of this Act to have been paid to any person as income for any year of assessment and—

(a) that amount is greater than the amount that has previously been deemed to have been paid to him as income for that year by virtue of this Part of this Act; or

(b) no amount has previously been so deemed to have been paid to him as income for that year;

an assessment or additional assessment may be made upon him for that year and tax charged accordingly or, on a claim being made for the purpose, any relief or additional relief to which he may be entitled shall be allowed accordingly.

(2) Where, on the completion of the administration of an estate, any amount is deemed by virtue of this Part of this Act to have been paid to any person as income for any year of assessment, and that amount is less than the amount that has previously been so deemed to have been paid to him, then—

(a) if an assessment has already been made upon him for that year, such adjustments shall be made in that assessment as may be necessary for the purpose of giving effect to the provisions of this Part of this Act which take effect on the completion of the administration, and any tax overpaid shall be repaid ;

(b) if—

(i) any relief has been allowed to him by reference to the amount which has been previously deemed as aforesaid to have been paid to him as income for that year ; and

(ii) the amount of that relief exceeds the amount of relief which could have been given by reference to the amount which, on the completion of the administration, is deemed to have been paid to him as income for that year ;

the relief so given in excess may, if not otherwise made good, be charged under Case VI of Schedule D and recovered from that person accordingly.

(3) Notwithstanding anything contained in the Income Tax Acts, the time within which an assessment or additional assessment may be made for the purposes of this Part of this Act, or an assessment may be adjusted for those purposes, or a claim for relief may be made by virtue of this Part of this Act, shall not expire before the end of the third year following the year of assessment in which the administration of the estate in question was completed.

(4) The General or Special Commissioners may by notice in writing require any person being or having been a personal representative of a deceased person, or having or having had an absolute or limited interest in the residue of the estate of a deceased person or in a part thereof, to furnish them (within such time as they may direct, not being less than twenty-eight days) with such particulars as they think necessary for the purposes of this Part of this Act, and if that person without reasonable excuse fails to comply with the notice, he shall be liable to a penalty not exceeding fifty pounds, and, after judgment has been given for that penalty, to a further penalty of the like amount for each day during which that failure continues.

#### *Interpretation of Part III.*

35.—(1) The following provisions of this section shall have effect for the purpose of the interpretation of the foregoing provisions of this Part of this Act.

(2) A person shall be deemed to have an “absolute interest” in the residue of the estate of a deceased person, or in a part thereof, if and so long as the capital of the residue or of that part thereof, as the case may be, would, if the residue had been ascertained, be properly payable to him, or to another in his right, for his benefit, or is properly so payable, whether directly by the personal representatives or indirectly through a trustee or other person.

(3) A person shall be deemed to have a “limited interest” in the residue of the estate of a deceased person, or in a part thereof, during any period, being a period during which he has not an absolute interest in the residue

or in that part thereof, as the case may be, where the income of the residue or of that part thereof, as the case may be, for that period would, if the residue had been ascertained at the commencement of that period, be properly payable to him, or to another in his right, for his benefit, whether directly or indirectly as aforesaid.

(4) The expression "personal representatives" means, in relation to the estate of a deceased person, his personal representatives as defined in relation to England by section fifty-five of the Administration of Estates Act, 1925, and persons having in relation to the deceased under the law of another country any functions corresponding to the functions for administration purposes under the law of England of personal representatives as so defined, and references to personal representatives as such shall be construed as references to the personal representatives in their capacity as having such functions as aforesaid.

(5) The expression "specific disposition" means a specific devise or bequest made by a testator, and includes the disposition of personal chattels made by section forty-six of the Administration of Estates Act, 1925, and any disposition having, whether by virtue of any enactment or otherwise, under the law of another country an effect similar to that of a specific devise or bequest under the law of England.

Real estate included (either by a specific or general description) in a residuary gift made by the will of a testator shall be deemed to be a part of the residue of his estate and not to be the subject of a specific disposition.

(6) The expression "charges on residue" means, in relation to the estate of a deceased person, the following liabilities properly payable thereout and interest payable in respect of those liabilities, that is to say—

(a) funeral, testamentary and administration expenses and debts;

(b) general legacies (including in the case of an intestacy the sum of one thousand pounds charged by virtue of section forty-six of the Administration of Estates Act, 1925), demonstrative legacies and annuities; and

(c) any other liabilities of his personal representatives as such;

but, in the case of any such liabilities which, as between persons interested under a specific disposition or in such a legacy as aforesaid or in an annuity and persons interested in the residue of the estate, fall exclusively or primarily upon the property that is the subject of the specific disposition or upon the legacy or annuity, includes only such part (if any) of those liabilities as falls ultimately upon the residue.

(7) References to the "aggregate income of the estate" of a deceased person for any year of assessment shall be construed as references to the aggregate income from all sources for that year of the personal representatives of the deceased as such, treated as consisting of—

(a) any such income which is chargeable to United Kingdom Income Tax by deduction or otherwise, such income being computed at the amount on which that tax falls to be borne for that year, and

(b) any such income which would have been so chargeable if it had arisen in the United Kingdom to a person resident and ordinarily resident therein, such income being computed at the full amount thereof actually arising during that year, less such deductions as would have been allowable if it had been charged to United Kingdom Income Tax,

but excluding any income from property devolving on the personal representatives otherwise than as assets for payments of the debts of the deceased.



(8) The expressions "United Kingdom estate" and "foreign estate" mean respectively, as regards any year of assessment—

- (a) an estate the income whereof comprises only income which either has borne United Kingdom Income Tax by deduction or in respect of which the personal representatives are directly assessable to United Kingdom Income Tax, not being an estate any part of the income of which is income in respect of which the personal representatives are entitled to claim exemption from United Kingdom Income Tax by reference to the fact that they are not resident, or not ordinarily resident, in the United Kingdom; and
- (b) an estate other than a United Kingdom estate.

(9) In a case in which different parts of the estate of a deceased person are the subjects respectively of different residuary dispositions, this Part of this Act shall have effect in relation to each of those parts, with the substitution for references to the estate of references to that part of the estate, and for references to the personal representatives of the deceased as such of references to his personal representatives in their capacity as having the functions referred to in subsection (4) of this section in relation to that part of the estate.

(10) References to sums paid or payable in respect of an absolute or limited interest in the residue of the estate of a deceased person, or in a part thereof, shall, in the application of this Part of this Act for the purposes of Sur-tax, be construed as excluding any sum paid or payable in discharge of any legacy duty charged in respect of that absolute or limited interest.

(11) The expression "standard tax" means United Kingdom Income Tax at the standard rate.

(12) References to sums paid include references to assets that are transferred or that are appropriated by a personal representative to himself, and to debts that are set off or released; references to sums payable include references to assets as to which an obligation to transfer or a right of a personal representative to appropriate to himself is subsisting on the completion of the administration and to debts as to which an obligation to release or set off, or a right of a personal representative so to do in his own favour, is then subsisting; and references to amount shall be construed, in relation to such assets, as references to the value thereof at the date on which they were transferred or appropriated, or at the completion of the administration, as the case may require, and, in relation to such debts, as references to the amount thereof.

*Application of Part III to Scotland and Northern Ireland.*

36.—(1) For the purpose of the application of this Part of this Act to Scotland—

- (i) any reference to the completion of the administration of an estate shall be construed as a reference to the date at which, after discharge of, or provision for, liabilities falling to be met out of the deceased's estate (including, without prejudice to the foresaid generality, debts, legacies immediately payable, and legal rights of surviving spouse or children) the free balance held in trust for behoof of the residuary legatees has been ascertained;
- (ii) for paragraph (b) of subsection (1) of section thirty-two of this Act, the following paragraph shall be substituted—

"(b) the amount of any of the aggregate income of the estate for that year to which a person has become entitled by virtue of a specific disposition ;"

- (iii) the expression "real estate" means heritable estate;
- (iv) for any reference to the sum of one thousand pounds charged by virtue of section forty-six of the Administration of Estates Act, 1925, there shall be substituted a reference to the sum of five hundred pounds to which a widow is entitled by virtue of the Intestate Husband's Estate (Scotland) Act, 1911;
- (v) the expression "charges on residue" shall include in addition to the liabilities specified in subsection (6) of the last foregoing section any sums required to meet claims in respect of legal rights by surviving spouse or children.

(2) For the purpose of the application of this Part of this Act to Northern Ireland, for any reference to the sum of one thousand pounds charged by virtue of section forty-six of the Administration of Estates Act, 1925, there shall be substituted a reference to the sum of five hundred pounds to which a widow is entitled by virtue of section two of the Intestates' Estates Act, 1890.

#### *Commencement of Part III.*

37.—(1) This Part of this Act shall have effect, in relation to amounts deemed by virtue thereof to have been paid as income—

- (a) in the case of amounts so deemed by virtue of section thirty of this Act, or by virtue of subsection (3) of section thirty-three of this Act, for the purpose of assessment to Income Tax and reliefs for the year 1937-38 and subsequent years; and
- (b) in the case of amounts so deemed by virtue of section thirty-one of this Act, for the purpose of assessment to Income Tax and reliefs for the year 1938-39 and subsequent years;

and shall apply in relation to the estate of a deceased person whether he died before or after the commencement of the year 1937-38 or the year 1938-39, as the case may be:

Provided that no income shall be charged to standard tax by virtue of this Part of this Act for the year 1937-38 in a case to which paragraph (a) of this subsection applies, but Sur-tax shall be assessed and charged as if any income which would, but for this proviso, have been charged as aforesaid had in fact been so charged.

(2) Section thirty of the Finance Act, 1922 (which relates to cases where a charity is entitled to a residue) shall not apply to income for the year 1938-39 or for any subsequent year.

(3) Any relief given to any person before the commencement of this Act in respect of any income in respect of which that person is entitled to relief by virtue of this Part of this Act shall be taken as having been given on account of the relief to which he is so entitled.

## APPENDIX XIII.

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### RELIEF IN RESPECT OF DIMINUTION OF EARNED

INCOME (§ 11—(No. 2) 1939 ; § 23—1940 ;

§ 8—1941 ; § 25—1942 ; § 17—1943 ; § 21—1944 ;

§ 19—(No. 2) 1945 ; § 25—1946).

An individual whose earned income was reduced through war conditions suffered unduly from the assessment being based on the income of the previous year, owing to the heavy increase in the standard rate.

Up to 1945-46, however, if a claim was made not later than 5th April following the end of the year of assessment, proving that owing to circumstances directly or indirectly connected with the war, the individual's actual earned income for the year of assessment did not exceed eighty per cent. of his earned income as assessed for that year, relief was given, computed as follows :—

- (a) The Income Tax (*excluding* Sur-tax) payable on the earned income as originally assessed was calculated.
- (b) The Income Tax (*excluding* Sur-tax) which would be payable on an assessment for the year based on the actual earned income for that year was calculated.
- (c) If the actual earned income of the preceding year of assessment exceeded the earned income as assessed for that year the *additional* Income Tax (*including* Sur-tax) which would have been payable had the earned income for that year been assessed on the actual income instead of on the normal basis was calculated.
- (d) The relief was the excess of (a) over (b), reduced by (c).
- (e) In computing the Sur-tax payable for the year of assessment the actual earned income for that year, instead of the preceding year's income was included in arriving at the total income, *i.e.*, relief from Sur-tax was the difference between the amount normally payable and this amended amount.
- (f) If (c) exceeded (a) - (b), the balance was deductible from the relief under (e).

The relief was given, so far as possible, from the second instalment of standard rate tax for the year of assessment, any balance being given by way of repayment.

Where the actual earned income for the year of assessment, although less than the earned income as originally assessed, was more than 80% thereof, the relief from standard rate tax, where claimed, was computed as if the actual earned income had been exactly 80% of the earned income as originally assessed. From the relief so found was then deducted the excess of the actual income over 80% of the earned income as assessed.

In such cases the relief from Sur-tax was such reduction in the amount of Sur-tax payable as would result from including in the total income 80% instead of the full amount of the earned income as originally assessed. If the excess of the earned income over 80% of the assessed earned income exceeded the relief available for Income Tax, the difference was set against the relief for Sur-tax.

Where relief for diminution of earned income was claimed, any losses or wear and tear allowances brought forward were deducted from the substituted assessment based on the actual earned income for the year.

The relief granted under this section could not be such as would reduce the amount of tax payable by an individual below the amount of tax which he was entitled to deduct from annual charges.

The actual profits of a firm assessed under Sch. B must be found by preparing accounts. The Sch. B assessment is obviously not the actual profits.

#### Illustration (1).

An individual's income was as follows :—

Share of profits as acting partner—

Year to 31st December, 1940	..	..	£400
ditto 1941	..	..	500
ditto 1942	..	..	200
ditto 1943	..	..	300

Profits of business carried on by wife—

Year to 31st March, 1941	..	..	£600
ditto 1942	..	..	700
ditto 1943	..	..	800

Business carried on as sole trader—

Year to 30th June, 1940	..	..	£1,000
ditto 1941	..	..	1,200
ditto 1942	..	..	1,300
ditto 1943	..	..	100

A loss of £300 was brought forward from 1940-41 (incurred 1938-39).

Wear and Tear—brought forward from 1940-41 .. £900

due for 1941-42 .. .. 250

due for 1942-43 .. .. 230

Director's Fees—Year to 5th April, 1941 .. .. £500

1942 .. .. 400

1943 .. .. 100

Unearned income from partnership £200 per annum.

Dividends taxed at source £1,000 per annum.

Annual payments £100 per annum.

ASSESSMENTS.		ACTUAL INCOME.	
	1941-42.	1941-42.	1942-43.
Partnership .. ..	£ 400	£ 500	500
Wife's Business .. ..	600	700	500
Sole Trader .. ..	£1,000	£1,200	£100
Less Wear and Tear .. £250			
ditto brought forward 900	1,150	£1,275	£ of £1,300 + $\frac{1}{2}$ of £100 = £100
		900	500
Less brought forward		1,150	
Director's Fees .. ..	500	400	100
Total Assessments ..	1,500	1,600	1,100
Add Unearned Income ..	1,200	1,200	1,200
	2,700	2,800	2,300
Deduct Annual Payments	100	100	100
Statutory Total Income ..	£2,600	£2,700	£2,200

726 EARNED INCOME DIMINUTION—RELIEF.

		1941-42	1942-43
Original Assessments on earned income.			
Earned Income .. ..		£1,500	£2,120
Less Allowances—			
Earned .. ..	£150	£150	
Personal (married) .. ..	140	140	
Additional Personal .. ..	45	80	
2 Children .. ..	100	100	
	435		470
	<u>£1,065</u>		<u>£1,650</u>
		£ s. d.	£ s. d.
£165 at 6s. 6d.	53 12 0	£165 at 6s. 6d.	53 12 6
900 at 10s. 0d.	450 0 0	1,485 at 10s. 0d.	742 10 0
	503 12 6		796 2 6
Life Assurance Relief (say)	10 0 0		10 0 0
	<u>£493 12 6</u>		<u>£786 2 6</u>

Since the actual earned income for 1942-43 (£1,100) does not exceed 80% of the earned income as assessed (£2,120) relief is due as follows:—

(a) Tax as assessed, 1942-43 .. ..	£	£	£ s. d.
			786 2 6
(b) Tax on actual earned income .. ..	1,100		
Less Allowances—			
Earned income .. ..	110		
Personal .. ..	140		
Additional Personal .. ..	80		
Children .. ..	100		
	430		
	<u>£670</u>		
	£ s. d.		
£165 at 6s. 6d.	53 12 6		
505 at 10s. 0d.	252 10 0		
	306 2 6		
Life Assurance Relief ..	10 0 0		
	<u>296 2 6</u>		
	490 0 0		
(c) Less Additional Standard Rate Tax for 1941-42, £100 at 10s. 0d. ..	50 0 0		
Additional Sur-tax for 1941-42, £100 at 2s. 3d. .. ..	11 5 0		
	<u>61 5 0</u>		
Relief .. ..	<u>£428 15 0</u>		

Since the second instalment due 1st July, 1943, is £303 1s. 3d., it will be discharged and the balance of £36 13s. 9d. repaid.

NOTE.—The practice was to regard the adjusted profits for the accounting year ending in the year of assessment, as the profits of the year of assessment,

# APPENDIX XIII.

but only where the accounts were made up to 31st December, or to a date thereafter and not later than 5th April, and provided the actual income for the preceding year was computed on a similar basis. The taxpayer could, however, insist on splitting accounts to find the income of the year of assessment.

## Illustration (2).

On computations similar to the above, it is found that the relief due for 1939-40 is £215, but the additional Income Tax and Sur-tax for 1938-39 is £240. The assessment of Sur-tax, by reference to actual earned income for 1939-40, however, reduces the Sur-tax for 1939-40 by £78. Accordingly, the Income Tax for 1939-40 will be payable in full, but the relief for Sur-tax will be reduced to £78 - (£240 - £215) = £53.

## Illustration (3).

An individual's income was as follows :—

As assessed.		Actual.	
	1940-41	1941-42	
Earned ..	£700	£800	£760
Unearned ..	2,000	2,000	2,000
	<u>£2,700</u>	<u>£2,800</u>	<u>£2,760</u>
Relief—1941-42.			
Actual diminution of earned income	£800 - £650	..	..
			<u>£150</u>
Regarded as £800 - 80% of £800	..	..	..
Less Earned Income Allowance	..	..	..
			<u>160</u>
			<u>16</u>
			<u>£144</u>
Relief—£144 at 10s. 0d. ..	..	..	..
Less Excess of actual earned income over 80% of earned income as originally assessed (£650 - £640)	..	..	..
			<u>72 0 0</u>
			<u>62 0 0</u>
Less Additional standard rate tax 1940-41—			
Additional earned income ..	£60		
Less Earned Income Allowance ..	10		
	<u>£50 at 8s. 6d. ..</u>	<u>£21 5 0</u>	
Additional Sur-tax £60 at 2s. 3d. ..		<u>6 15 0</u>	
			<u>28 0 0</u>
Net relief ..	..	..	<u>£34 0 0</u>

Sur-tax, 1941-42, will be payable on £2,640 instead of on £2,800, i.e., the relief for Sur-tax will be such as would result from including in the total income only 80% of the £800 earned income instead of the full amount of £800 originally assessed.

## APPENDIX XIV.

RETIREMENT AND OTHER BENEFITS FOR  
DIRECTORS AND EMPLOYEES.

(FINANCE ACT, 1947.)

*Charge to tax in respect of provision for retirement or other benefits to directors and employees of bodies corporate.*

19.—(1) Subject to the exemptions and provisions contained in the next succeeding section, where pursuant to a scheme for the provision of future retirement or other benefits for persons consisting of or including directors or employees of a body corporate (in this and the next four succeeding sections referred to as a "retirement benefits scheme") the body corporate in any year of assessment pays a sum with a view to the provision of any such benefits for any director or employee thereof, then (whether or not the accrual of the benefits is dependent on any contingency),—

- (a) the sum paid, if not otherwise chargeable to income tax as income of the director or employee, shall be deemed for all the purposes of the Income Tax Acts to be income of that director or employee for that year of assessment and assessable to income tax under Schedule E; and
- (b) where the payment is made under such an insurance or contract as is mentioned in section thirty-two of the Income Tax Act, 1918 (which relates to relief for life insurance premiums, etc.), relief, if not otherwise allowable, shall be given to him under that section in respect of the payment to the extent, if any, to which such relief would have been allowable to him if the payment had been made by him and the insurance or contract under which the payment is made had been made with him.

(2) Subject to the exemptions and provisions contained in the next succeeding section, where—

- (a) an agreement is in force between a body corporate and a director or employee thereof for the provision for him of any future retirement or other benefits afforded by a retirement benefits scheme, or a person is serving as a director or employee of a body corporate in connection wherewith there is a retirement benefits scheme relating to persons of the class within which he falls under which any such benefits will be provided for him; and
- (b) the body corporate does not, or does not fully, secure the provision of the benefits by the payment of such sums as are mentioned in the preceding subsection; and
- (c) the circumstances in which the benefits are to accrue are not such as will render the benefits assessable to income tax under Schedule E as emoluments of his office as a director or of his employment,

then (whether or not the accrual of the benefits is dependent on any contingency), in each year of assessment in which the agreement is in force or the director or employee is serving as aforesaid, up to and including the year of assessment in which the benefits accrue or there ceases to be any possibility of the accrual thereof, a sum equal to the annual sum which the



body corporate would have had to pay in that year under a contract with a third person which secured the provision by that third person of those benefits or, as the case may be, of those benefits so far as not already secured by the payment of such sums as are mentioned in the preceding subsection, shall be deemed for all the purposes of the Income Tax Acts to be income of the director or employee for that year and assessable to income tax under Sch. E.

(3) Where the body corporate pays any sum as mentioned in subsection (1) of this section in relation to several directors or employees, the sum so paid shall, for the purpose of that subsection, be apportioned among them by reference to the separate sums which would have had to be paid to secure the separate benefits to be provided for them respectively, and the part of the sum apportioned to each of them shall be deemed for that purpose to have been paid separately in relation to that one of them.

*Exemptions from charge to tax under the preceding section.*

20.—(1) The following payments shall be exempted from the operation of subsection (1) of the last preceding section, that is to say—

- (a) payments made pursuant to a statutory superannuation scheme, or made to a superannuation fund approved (whether in whole or in part) by the Commissioners of Inland Revenue for the purposes of section thirty-two of the Finance Act, 1921;
- (b) payments made pursuant to an excepted provident fund or staff assurance scheme or other similar scheme (as defined in section twenty-three of this Act);
- (c) payments made by way of premium pursuant to a scheme the benefits whereunder are secured by premiums payable by the body corporate, with or without contributions by the directors or employees affected, under life or endowment assurance or life annuity contracts, being a scheme which was in operation before the sixth day of April, nineteen hundred and forty-seven, and which is not confined, or substantially confined, to directors and persons, who, not being directors, are remunerated at a rate exceeding two thousand pounds a year or to directors or to such persons.

(2) Neither subsection (1) nor subsection (2) of the last preceding section shall apply so as to cause any sum to be deemed to be income as therein mentioned where the retirement benefits scheme in question is one under which the main benefit afforded to each of the persons to whom the scheme relates is the provision for him of a pension or annuity for his life, and either—

- (a) that scheme was in operation before the sixth day of April, nineteen hundred and forty-four; or
- (b) that scheme is for the time being approved by the said Commissioners under the next succeeding section.

(3) Where in respect of the provision for a director or employee of any future retirement or other benefits a sum has been deemed to be income of his by virtue either of subsection (1) or of subsection (2) of the last preceding section, and subsequently the director or employee proves to the satisfaction of the said Commissioners that no payment in respect of, or in substitution for, the benefits has been made and that some event has occurred by reason whereof no such payment will be made, and claims relief under this subsection within three years from the time when that event occurred, they shall give relief in respect of tax on that sum by repayment or otherwise as may be appropriate; and if the director or employee satisfies the said Commissioners as aforesaid in relation to some particular part of the benefits but not the whole thereof, they may give such relief as may seem to them just and reasonable.

(4) Where apart from this subsection any sum would be deemed, by virtue either of subsection (1) or of subsection (2) of the last preceding section, to

be income of an employee for any year of assessment, but, by reason of his exercising his employment outside the United Kingdom he is not assessable to income tax under Schedule E in respect of the emoluments of his employment for that year, that subsection shall not apply so as to cause that sum to be deemed to be income of his for that year.

*Approval of retirement benefit schemes.*

21.—(1) Subject to the provisions of the next succeeding section the Commissioners of Inland Revenue shall approve a retirement benefits scheme for the purpose of subsection (2) of the last preceding section unless it appears to them that the scheme does not fall within the said subsection (2) by reason of the fact that the main benefit afforded thereby is not such as is therein mentioned, or that, although the main benefit is such as aforesaid, the scheme fails to satisfy some one or more of the following conditions, that is to say—

- (a) that that benefit will accrue only on retirement at a specified age or on earlier retirement through incapacity or on death ;
- (b) that the nature of the benefits afforded by the scheme is the same in relation to all the persons to whom the scheme relates ;
- (c) that the proportion between the value of the pensions or annuities provided for by the scheme, in so far as they are not commutable, and the value of all other benefits afforded thereby, including the value of so much, if any, of the said pensions or annuities as is commutable, is reasonably comparable to the proportion between the values of such benefits respectively as are usually afforded by statutory superannuation schemes ;
- (d) that the aggregate value of the benefits, of whatever nature, afforded by the scheme is reasonably comparable to the aggregate value of the benefits usually afforded by statutory superannuation schemes in like circumstances ;
- (e) that the pensions or annuities provided for by the scheme are not assignable, either in whole or in part ; and
- (f) that no service of a person, in whatever capacity, rendered by him while he is a controlling director of the body corporate is taken into account for any of the purposes of the scheme :

Provided that the said Commissioners may, if they think fit, having regard to the facts of the particular case, approve a scheme the main benefit afforded whereby is such as is mentioned in subsection (2) of the last preceding section notwithstanding that it may not, in one or more respects, satisfy the whole of the aforesaid conditions.

(2) Where the said Commissioners have given their approval to a scheme, they may at any time, by notice in writing to the body corporate in question, withdraw their approval on such grounds and as from such date as may be specified in the notice.

(3) In the case of a scheme in existence at the passing of this Act the main benefit afforded whereby is not then such as is mentioned in subsection (2) of the last preceding section, or which does not then satisfy the conditions specified in subsection (1) of this section, but which is so altered before the sixth day of April, nineteen hundred and forty-eight, or within such further time as the said Commissioners may allow, as to be approvable under this section, approval thereof after the sixth day of April, nineteen hundred and forty-seven, shall, if the said Commissioners so direct, be deemed to have had effect as from that day.

*Aggregation and severance of schemes.*

22.—(1) References in this section, in the last three preceding sections, and in the next succeeding section, to a retirement benefits scheme shall be construed in accordance with the following provisions, that is to say—

- (a) references to such a scheme shall, in relation to a deed, agreement, series of agreements, or other arrangements providing for retirement or other benefits for persons of two or more classes, be construed as references to so much thereof as relates to persons of a single class, and accordingly a deed, agreement, series of agreements or other arrangements so providing shall be treated for the purposes of those sections as constituting two or more retirement benefits schemes relating respectively to the different classes ;
  - (b) references to such a scheme include references to a deed, agreement, series of agreements, or other arrangements providing for retirement or other benefits for persons consisting of or including a director or employee, or directors or employees, of a body corporate (or, in a case falling within the preceding paragraph, to so much thereof as relates to a person or persons of any one class), notwithstanding that it or they relates or relate only to a small number of directors or employees or to a single director or employee.
- (2) For the purpose—
- (a) of determining, in the case of a retirement benefits scheme which was in operation before the sixth day of April, nineteen hundred and forty-four, whether the scheme falls within subsection (2) of section twenty of this Act as respects the nature of the main benefit afforded thereby, and
  - (b) of determining, in the case of a retirement benefits scheme submitted for the approval of the Commissioners of Inland Revenue, whether the scheme so falls and whether the conditions specified in subsection (1) of the last preceding section are satisfied.

the scheme shall be considered in conjunction with any other retirement benefits scheme or schemes subsisting in connection with the body corporate and relating to persons of the class to which the scheme in question relates, and—

(i) if the main benefit afforded by all of those schemes taken together is such as is mentioned in subsection (2) of section twenty of this Act, each of them shall be taken to fall within that subsection as respects the nature of the main benefit afforded thereby, and, if it is not, none of them shall be taken so to fall ; and

(ii) if the said conditions are satisfied in the case of all of them taken together, those conditions shall be taken to be satisfied in the case of each of them, and, if not, those conditions shall be taken to be satisfied in the case of none of them.

(3) The said Commissioners may, if they think fit,—

- (a) approve a part of a retirement benefits scheme ; or
- (b) approve such a scheme notwithstanding that, having regard to another such scheme subsisting in connection with the body corporate the scheme in question is to be treated by virtue of the last preceding subsection as not falling within subsection (2) of section twenty of this Act or as not satisfying the conditions aforesaid ;

and where under this subsection the said Commissioners approve a part of a scheme, neither subsection (1) nor subsection (2) of section nineteen of this Act relating to retirement or other benefits shall apply so as to cause any sum to be deemed to be income of a director or employee by reference to the provision for him of benefits afforded by that part of the scheme or of any part of such benefits.

*Supplementary provisions as to retirement or other benefits and application to unincorporated societies, etc.*

23.—(1) In this and the last four preceding sections, except where the context otherwise requires, the following expressions have the meanings hereby respectively assigned to them, that is to say—

"controlling director" means a director of a company, the directors whereof have a controlling interest therein, who is the beneficial owner of, or able, either directly or through the medium of other companies or by any other indirect means, to control, more than five per cent. of the ordinary share capital of the company, and for the purposes of this definition the expressions "company" and "ordinary share capital" have the same meanings as they have for the purposes of the Fourth Schedule to the Finance Act, 1937;

"director" means—

(a) in relation to a body corporate the affairs whereof are managed by a board of directors or similar body, a member of that board or similar body;

(b) in relation to a body corporate the affairs whereof are managed by a single director or similar person, that director or person;

(c) in relation to a body corporate the affairs whereof are managed by the members themselves, a member of the body corporate, and includes any person who is to be or has been a director;

"employee," in relation to a body corporate, includes any person taking part in the management of the affairs of the body corporate who is not a director, and includes a person who is to be or has been an employee;

"excepted provident fund or staff assurance scheme or other similar scheme" means so much as relates to persons remunerated at a rate of two thousand pounds a year, or at a less rate, of any retirement benefits scheme as to which the following conditions are satisfied, that is to say—

(a) that the sums paid by the body corporate pursuant to the scheme in question in respect of any person for any period do not exceed ten per cent. of his remuneration for that period and do not exceed one hundred pounds in the case of a period of a year or a correspondingly less or greater amount in the case of a shorter or longer period; and

(b) that no other retirement benefits scheme which relates to employees of the body corporate who are of the class to which the scheme in question relates, and who are remunerated as aforesaid, is subsisting for the time being, or, if there is any such other scheme subsisting that it (so far as it relates to persons remunerated as aforesaid) and the scheme in question taken together satisfy the requirement specified in paragraph (a) of this definition;

"retirement or other benefit," means any pension, annuity, lump sum, gratuity or other like benefit to be given on retirement, or in anticipation of retirement, or, in connection with past service, after retirement, or to be given on or in anticipation of or in connection with any change in the nature of the service of the person in question, except that it does not include any pension, annuity, lump sum, gratuity or other like benefit which is to be afforded solely by reason of the death or disability of a person occurring during his service, and for no other reason;

"service" means service as an employee or director of the body corporate in question, and "retirement" shall be construed accordingly;

"statutory superannuation scheme" means a scheme set up by or approved under any enactment relating to superannuation or set up by or approved under any regulations relating to superannuation made under any enactment by any Minister or government department, and for the purposes of this definition, the expressions "enactment," "Minister" and "government department" include respectively an enactment of the Parliament of Northern Ireland, a Northern Ireland Minister and a Northern Ireland government department.

(2) Where an alteration has been made in a retirement benefits scheme at any time after the fifth day of April, nineteen hundred and forty-seven, the scheme shall, for the purposes of this and the last four preceding sections be deemed to have become a new scheme coming into being on the date of the alteration.

Provided that this subsection shall not apply to an alteration approved by the Commissioners of Inland Revenue.

(3) Any reference in this or the last four preceding sections to the provision for a person of retirement or other benefits includes a reference to the provision of benefits payable to that person's spouse, children, dependants or personal representatives, and any reference therein to the provision for a person of a pension or annuity for his life includes a reference to the provision (either in addition or as an alternative to the pension or annuity payable for his life) of a pension or annuity payable to that person's spouse or to any child or dependant of that person for the life of the spouse, child or dependant.

(4) Any reference in this or the last four preceding sections to the provision of retirement or other benefits, or of a pension or annuity, by a body corporate includes a reference to the provision thereof by means of a contract with a third person.

(5) It shall be the duty of a body corporate—

- (a) to deliver to the surveyor, within the time specified in this subsection, particulars of any retirement benefits scheme subsisting in connection with the body corporate on the sixth day of April, nineteen hundred and forty-seven, or coming into being after that date, other than a scheme referred to in subsection (1) of section twenty of this Act relating to retirement or other benefits, and
- (b) when required so to do by notice given by the surveyor, to furnish within the time limited by the notice such further particulars as he may require with regard to any retirement benefits scheme subsisting in connection with the body corporate or to the persons to whom it relates.

and the provisions of section one hundred and seven of the Income Tax Act, 1918 (which relates to failure to deliver lists, declarations and statements) shall apply in relation to the particulars required to be delivered by or under this subsection as they apply in relation to any list, declaration or statement required to be delivered by any such notice as is referred to in that section.

The time for delivery of particulars under paragraph (a) of this subsection shall be—

- (a) in the case of a scheme that came into being before the passing of this Act, six months beginning with the date of the passing of this Act;
- (b) in the case of a scheme coming into being after the passing of this Act, three months beginning with the date of its coming into being.

(6) This and the last four preceding sections shall apply in relation to unincorporated societies or other bodies as they apply in relation to bodies corporate:

Provided that the reference in this subsection to unincorporated societies or other bodies shall be deemed not to include a reference to individuals in partnership.

## APPENDIX XV.

### EXTRA STATUTORY TAX CONCESSIONS—II.

*Reprinted from the White Paper (Cmd.6559), "A List of Extra-Statutory Wartime Concessions given in the Administration of Inland Revenue Duties."*

The wartime concessions described below are of general application, but it must be borne in mind that in a particular case there may be special circumstances which will require to be taken into account in considering the application of the concession.

#### INCOME TAX.

##### 1. INCOME FROM LAND, HOUSES, ETC.

###### (i) Abatement of rent.

Where owing to war conditions rent is abated, waived or temporarily reduced, the tax payable is computed not by reference to the annual value as assessed under Schedule A, but by reference to the lower figure of the rent. (Tax under Schedule B where payable in such a case is similarly computed by reference to the rent.)

###### (ii) Property in "evacuation," "defence" or "protected" areas.

- (a) Relief from Income Tax Schedule A is allowed by law where a house is unoccupied (unless rent remains payable), but in strictness a house is not regarded as unoccupied if it continues furnished and ready for occupation.

The relief is given notwithstanding that the house continues furnished and ready for occupation in the cases of:—

owner-occupiers of property in an evacuation area who either under compulsion or in compliance with an official appeal relating to the area have left the area;

owner-occupiers of property in a defence or protected area who ordinarily reside outside the area and are not permitted to visit (for residence) their properties in that area;

alien owner-occupiers of property in a protected area from which aliens are excluded;

licensed premises in an evacuation area which are closed.

- (b) Where the owner-occupier continues to live in his house in an evacuation, defence or protected area, any reduction of the rating valuation is followed for Income Tax purposes without formal reduction of the Schedule A assessment.

###### (iii) Damaged properties.

Where an owner-occupied property is seriously damaged by enemy action but is rendered only partly or temporarily uninhabitable, relief from Income Tax Schedule A is allowed in proportion to any relief that may be given from rates.

## 2. TEMPORARY RESIDENCE IN THE UNITED KINGDOM OWING TO WAR CONDITIONS.

Income from United Kingdom sources is, in general, chargeable to Income Tax wherever the recipient is resident, while a person resident in the United Kingdom is liable also on income arising from sources outside the United Kingdom (either on the full amount of the income or on the amount remitted to this country, according to the taxpayer's circumstances or the nature of the income).

The following relaxations of the strict liability are made :—

(i) Members of Allied, Dominion or Colonial Forces, or Mercantile Marine or recognised welfare organisations attached thereto.

Members of these Forces or organisations who have become temporarily resident here by reason of their service are treated as not resident for Income Tax purposes and are thereby exempted from tax on any income arising to them from sources outside the United Kingdom.

(ii) Persons who have come to the United Kingdom to join the Armed Forces of the Crown or the Mercantile Marine or the British Red Cross.

Where such persons have become temporarily resident here by reason of their service, they are treated as not resident for Income Tax purposes and are exempted from tax on income arising to them from sources outside the United Kingdom.

(iii) Refugees.\*

(a) In the case of individuals who have become temporarily resident in the United Kingdom because of enemy occupation of their home country, income from sources outside the United Kingdom is dealt with as follows :—

as regards *Allied Nationals* no tax is charged ;

as regards *individuals domiciled in the Channel Islands* tax is charged at the appropriate Channel Island rate.

(b) In the case of companies the central management and control of which was previously abroad but has been transferred to the United Kingdom because of enemy occupation of the home country and which have consequently become temporarily resident in the United Kingdom, profits from trading operations carried on abroad and income from foreign investments are dealt with as follows :—

as regards *Allied companies* no tax is charged ;

as regards *Channel Island and Colonial investment companies* and trading companies which carried on trading operations in the place in which the central management and control was previously situate, tax is charged at the appropriate Channel Island or Colonial rate, and not at the United Kingdom rate of tax, subject to the condition that any distributions by way of dividends or interest to United Kingdom shareholders or debenture holders are charged at the United Kingdom rate.

(iv) *Allied shipping concerns*.\*

Agreements made under Section 18 of the Finance Act, 1923, for the reciprocal exemption of the shipping profits of non-resident shipping concerns are treated as still operative in relation to Allied concerns which have become temporarily resident in the United Kingdom owing to enemy occupation of the home country. Exemption is given also in such cases of temporary residence although there is at the moment no formal agreement.

\* Withdrawn for 1947/48 onwards.

## 3. MEMBERS OF THE FORCES.

(i) No additional assessment on service pay is made for the penultimate year of service, whether the service is terminated by reason of death or by reason of demobilisation (cf. para. 5).

(ii) Where service in the Forces is terminated by death or demobilisation and the assessment for the final year of service would have been based on the preceding year's pay if the service had not terminated, the charge of tax for that year is computed on a part of the preceding year's pay proportionate to the period of service in the final year, if that part is less than the actual pay for the period. (This concession applies as from the year 1944-45.)

(iii) Where a member of the Forces dies on active service during the war, no action is taken to recover any tax outstanding in respect of service pay except to the extent that there is pay in hand to cover the tax payable.

(iv) Persons serving in the Forces who are paid from United Kingdom Government funds are liable to United Kingdom Income Tax on their service pay irrespective of where they lived before joining the Forces and whether they are serving in the United Kingdom or abroad, but in the cases of:—

- (a) members of Dominion or Colonial Forces who, because of the war, are transferred from the pay of the Dominion or Colony concerned to payment from United Kingdom funds;
- (b) residents of Dominions or Colonies who, during the war, join Forces associated with their Dominion or Colony which were not, before the war, paid from United Kingdom funds;
- (c) Dominion or Colonial Civil Servants who were in the pay of a Dominion or Colonial Government and are transferred to the British Forces for war purposes and become payable from United Kingdom funds; and
- (d) residents of Dominions or Colonies who have been recruited into the Royal Air Force direct in their Dominion or Colony under the Empire Air Training Scheme or the Air Ministry's Overseas Recruiting Scheme;

the charge to tax in respect of their service pay is abated so as not to exceed the tax which would be charged by reference to the appropriate Dominion or Colonial taxation code.

(v) Pending a review after the war of the taxation position of all allowances paid to members of the Forces, marriage allowances, lodging allowances, family allowances, and allowances in respect of children are in general exempted from tax.

(vi) If membership of a professional society is a condition of the tenure of a taxpayer's employment, he is entitled to claim in the assessment of his remuneration from that employment a deduction for his annual subscription to the society. Where a taxpayer whose employment has been the subject to such a condition has joined the Forces and during his war service continues to pay his annual subscription with a view to his ultimate return to his peacetime employment, a deduction for that subscription (if it cannot be given against pay received from his civilian employer during his service in the Forces) is allowed against his service pay.

(vii) The exemption from Income Tax given by Section 27 of the Finance Act, 1922, to payments made by the Ministry of Pensions to widows of members of the Forces in respect of their children is applied to similar payments in respect of children



made to "unmarried wives." (It is applied also to similar payments in respect of children made to widows and "unmarried wives" of members of the Mercantile Marine and to widows of civilians who have died from war injuries.)

#### 4. ALLIED MERCANTILE MARINE, ETC. \*

Members of the Allied Mercantile Marine who before the war were normally resident abroad and were based on foreign ports but have come to the United Kingdom because of the war and are sailing from British ports are not charged to United Kingdom Income Tax on their pay.

Similar treatment is allowed to civilian flying personnel of Allied nationality who before the war were normally resident abroad and were based on foreign aerodromes but because of the war are based on United Kingdom aerodromes and are flying on routes between this country and abroad.

#### 5. TRADES, EMPLOYMENTS, ETC., DISCONTINUED.

On the discontinuance of a trade, profession, vocation, office or employment, if the actual profits or income of the penultimate year exceed the amount of the assessment made for that year (on the preceding year basis), an additional assessment on the excess is by law required to be made.

This requirement is not enforced when the discontinuance of a trade, profession or vocation is due to :—

- (a) the taxpayer's joining the Armed Forces or the Mercantile Marine ;
- (b) his joining any Civil Defence Force in a full-time capacity ;
- (c) his death or disablement through war operations ;
- (d) the destruction of his business premises by enemy action or their occupation by the enemy.

Similarly, where in circumstances indicated under (a), (b) or (c) above a person has ceased to hold an office or employment, no additional assessment is made for the penultimate year, and similar treatment has been allowed where the employment of a merchant seaman has ceased because he has been taken prisoner of war. (For the Income Tax year 1944-45 and subsequent years, this concession is no longer operative in respect of offices and employments, as the income therefrom is now chargeable on the current year basis, except in the case of members of the Forces, as to whom see para. 3 (i).)

#### 6. REMITTANCES UNDER DEFENCE (FINANCE) REGULATIONS.

Persons whose liability to tax on income from a source abroad is limited to the amounts remitted to the United Kingdom and who are compelled under the Defence (Finance) Regulations to remit to the United Kingdom income from that source which would otherwise have been left abroad are assessed on the total remittances, but collection of tax is deferred on such amount of the compulsory remittances as is not expended or used in this country, but remains available, either in a specified bank account or in identified investments, for remittance abroad. Any part of such compulsory remittances which is remitted abroad not later than six months after the expiry of the Defence (Finance) Regulations will be treated as not having been remitted to the United Kingdom and an appropriate reduction in the assessment will then be made.

#### 7. FARMING.

Under Section 11 of the Finance Act, 1941, and Section 28 (1) of the Finance Act, 1942, where the annual value of the land occupied does not exceed a prescribed figure farming carried on by *an individual or partnership of individuals* is charged under Schedule B and not under Schedule D. The provisions do not in terms apply to the legal personal representatives of a deceased farmer, but where the farmer had been assessable under Schedule B,

\* Withdrawn for 1947/48 onwards.

assessment under Schedule B is continued for the period of administration unless the beneficiaries, if they had been in occupation of the farm during that period, would have been assessable under Schedule D. Similar treatment is given, by reference to the position of the life tenants, in the case of trusts created by will.

#### 8. EXCEPTIONAL DEPRECIATION ALLOWANCE.

Under Section 19 of the Finance Act, 1941, an "exceptional depreciation allowance" is given in respect of buildings, machinery or plant provided for the purposes of a trade since the beginning of 1937.

Under the section the allowance in the case of *machinery and plant* may be carried forward to later years in so far as effect cannot be given to it in a particular year. The section does not provide for a similar carry-forward in the case of *buildings* but it is given in practice.

#### 9. MANAGEMENT EXPENSES.

Under Section 33 of the Income Tax Act, 1918, life assurance companies, etc., which are charged to tax on interest, etc., by deduction or otherwise and not on profits under Case I of Schedule D are entitled to claim repayment of tax on management expenses.

Allowances for exceptional depreciation under Section 19 of the Finance Act, 1941, which would be proper in the computation on a Case I liability in respect of profits, and amounts payable for National Defence Contribution or Excess Profits Tax which would be allowable in a Case I computation, are treated as management expenses for the purposes of a claim under Section 33.

#### 10. INSURANCE IN RESPECT OF WAR DAMAGE RISKS.

Section 12 of the Finance (No. 2) Act, 1940, prohibits the allowance for Income Tax purposes of payments made in connection with certain war damage indemnity schemes. Premiums paid under the Indian War Risks (Factories) Insurance Ordinance, 1942, fall within the prohibition, but companies carrying on business in India and, because they are controlled in the United Kingdom, liable to United Kingdom Income Tax on their Indian profits, are allowed to deduct one-half of the premiums, that being roughly the excess of the payments made in India over the payments which would have been due if the property insured had been situate in the United Kingdom and had come within the provisions of the War Damage Act, 1943 (contributions and premiums payable under which are not allowable deductions for Income Tax purposes). Similar relief is allowed for the purposes of National Defence Contribution and Excess Profits Tax.

#### 11. PAYMENTS TO PART-TIME FIRE GUARDS.

The standard subsistence allowances paid under the Government scheme to part-time fire guards at business premises are not considered to constitute taxable remuneration. Where a part-time fire guard does duty as such outside his working hours at his place of employment and receives payment in respect of such duty at a rate greater than the standard subsistence rate applicable to his case, so much of the payment as corresponds to the standard subsistence allowance which would have been payable for the period of duty performed is excluded from assessment.

#### 12. MINERS : ALLOWANCES IN LIEU OF FREE COAL.

Income Tax is not charged on cash payments received during the war by miners from their employers in lieu of the free coal which they have been entitled to receive by virtue of their employment.

**13. CHRISTMAS PRESENTS IN KIND TO EMPLOYEES.**

Christmas presents in kind given by an employer to his subordinate employees are not treated as taxable remuneration, and this treatment has been extended to the presentation of Savings Certificates or Savings Stamps in lieu of such presents.

**14. SALVAGE AWARDS.**

Salvage awards are payments for services rendered and are taxable as such in the hands of the recipients. Salvage awards to officers and men of a ship not specifically employed on salvage work are not assessed to Income Tax if the awards are in respect of services rendered during the war.

**15. TIME LIMITS.**

Notice of claims to various Income Tax reliefs has, under the law, to be given within a prescribed period, usually twelve months from the end of the year of assessment to which the claim relates. When notice is not given within the prescribed period and the delay is due to war conditions, an extension of the time limit is given.

**NATIONAL DEFENCE CONTRIBUTION.****1. SEPARATE BUSINESSES : SET-OFF OF LOSS AGAINST PROFIT.**

Where two distinct businesses which are separately assessable are carried on by one person or firm a loss sustained in one business is allowed to be set off against profits made in the other business in a coincident chargeable accounting period.

**2. DIRECTOR-CONTROLLED COMPANIES : INTEREST, ETC., PAID TO WHOLE-TIME SERVICE DIRECTORS.**

Under the proviso to Rule 4, Fourth Schedule, Finance Act, 1937, no deduction is allowable under the Rule in respect of any interest, annuity or other annual payment paid to a director of a director-controlled company, or in respect of any royalty or rent so paid. Payments of such interest, etc., are, however, allowed as a deduction where the director is in a position corresponding to that of an employee, and satisfies the definition of a "whole-time service director" in Rule 13 (c), Fourth Schedule, Finance Act, 1937.

**3. BUSINESSES CARRIED ON BY TRUSTEES.**

Under Rule 12, Fourth Schedule, Finance Act, 1937, a deduction may be claimed, in the case of a business carried on by an individual or individuals in partnership, corresponding to that which could have been allowed in respect of directors' remuneration if the business had been carried on by a director-controlled company. The Rule requires that where any such deduction is made the Contribution is to be charged at the 5 per cent. rate applicable in the case of a business carried on by a body corporate.

Businesses carried on by individuals acting as trustees, executors or administrators are not strictly within the application of this Rule, but are treated as being within its application subject to the disallowance of:—

- (a) any remuneration paid to the trustees, executors or administrators (other than authorised charges for professional services rendered to the business), and
- (b) any remuneration paid to beneficiaries.

**4. DEDUCTION OF DIRECTORS' REMUNERATION.**

Rule 11, Fourth Schedule, Finance Act, 1937, limits the deduction to be allowed in computing the profits of a director-controlled company in respect of remuneration of the directors, other than whole-time service directors, and Rule 13 (c) of the Schedule defines the expression "whole-time

service director" as meaning a director who is required to devote substantially the whole of his time to the service of the company in a managerial or technical capacity and is not the beneficial owner of more than 5 per cent. of the ordinary share capital.

Directors prevented from devoting substantially the whole of their time to the service of a company because they are serving with the Armed Forces, Mercantile Marine or a Civil Defence Force, are not regarded as debarred on that account from being treated as whole-time service directors.

**5. DIRECTORS' REMUNERATION: TREATMENT OF SUMS RECEIVED FOR SERVICES IN TRADE OR PROFESSIONAL CAPACITY.**

The expression "remuneration of the directors" in Rule 11, Fourth Schedule, Finance Act, 1937, is interpreted as meaning the whole of any remuneration payable to the directors by way of salary, fees, bonus or commission, including any remuneration for services to the company which are of a secretarial, managerial, advisory or technical character. Exceptions are, however, made corresponding to those made in connection with the interpretation of the expression "directors' remuneration" for Excess Profits Tax purposes.

**6. EXPENDITURE ON MAINTENANCE OF PROPERTY.**

Expenditure on "maintenance" within the meaning of Rule 8 (2), No. V, Schedule A, Income Tax Act, 1918, by virtue of Section 25, Finance Act, 1924, is allowed as a deduction in computing the profits of property-owning concerns.

**7. MINERAL RIGHTS DUTY AND ROYALTIES WELFARE LEVY.**

Mineral Rights Duty and Royalties Welfare Levy are allowed as deductions in computing profits.

**8. INSURANCE COMPANIES WITH SUBSIDIARY INVESTMENT COMPANIES.**

Where the shareholders in such subsidiaries form part of the investments of the Insurance Company's Life Assurance Fund, the investments of the subsidiaries (or an appropriate proportion thereof) may be regarded as investments of the Life Assurance business of the parent company.

**9. DEFERRED REPAIRS AND RENEWALS.**

Relief is allowed on the same basis as for Excess Profits Tax.

SCHEDULE E—NEW AND DISCONTINUED SOURCES.

YEAR OF ASSESSMENT.	BASIS OF ASSESSMENT.
<i>New Sources.</i>	
(1) The year in which the employment commences.	The actual emoluments from the date of commencement to the following 5th April.
(2) The second year of the employment.	
(a) If the employment commenced on 6th April in the preceding year.	The emoluments of the previous (i.e., the first) year.
(b) If the employment commenced at a later date.	The actual emoluments of the year of assessment.
(3) Thereafter.	The emoluments of the preceding year of assessment.

### Discontinued Sources.

- |   |   |
|---|---|
| (4) The year in which the employment ceases.          | The actual emoluments from 6th April to the date of cessation.  |
| (5) The year before the cessation (penultimate year). | The emoluments of the preceding year of assessment, but the Commissioners of Inland Revenue increased the assessment to the emoluments of the actual year of assessment, though the taxpayer had no corresponding right of reduction. |

The same rules applied to any other sources assessable under Schedule E, on a preceding year basis, e.g., pensions, annuities or stipends. In other words, assessments were on "actual emoluments" until there was a full previous year, when the preceding year basis operated, but the taxpayer could claim to have the first "preceding year" assessment reduced to "actual." The assessment for the last year was "actual," and the Revenue increased that for the penultimate year to "actual."

### Illustration.

He was appointed manager of a company on 1st September, 1939, and died on 14th July, 1943. During the period his salary, including bonuses, was as follows :—

1st September, 1939, to 5th April, 1940	..	..	£600
Year ended 5th April	1941	..	1,500
" "	1942	..	1,300
" "	1943	..	1,800
6th April, 1943, to 14th July, 1943	..	..	500

The assessments under Schedule E would be as follows :—

1939-40—On the actual emoluments of the period .. .. .	£800
1940-41—Since the office first arose later than 6th April, 1939, the assessment is on the actual emoluments of the year of assessment .. .. .	1,500
1941-42—On the emoluments of the preceding year £1,500, but reduced to the emoluments of the year of assessment on a written claim being made not later than 5th April, 1943, <i>i.e.</i> .. .. .	1,300
1942-43—On the emoluments of the preceding year .. .. .	1,300
1943-44—On the actual emoluments of the year of assessment, since the employment ceased in this year .. .. .	500
An additional assessment of £500 will now be raised in respect of 1942-43 to bring the assessment up to the emoluments of that year .. .. .	
	1,800

What constituted a change of employment so as to give rise to the new and discontinued rules, was a question of fact. A change of employer operated as a change of employment, even where the only change in the proprietorship was the incorporation of a firm into a company (*Thomas v. C.I.R.* (1941), T.R. 69). Nevertheless, on a change of position under the same employer or a change of employer, with or without a change of duties (even if there has been temporary unemployment), assessments were normally continued on the preceding year basis, unless the taxpayer claimed that there was cessation of one employment and commencement of another. If, however, on a change of employer, there were both a considerable increase of remuneration and an advancement obviously out of the ordinary course, the rules for cessation and commencement were applied. A change would also be treated as a cessation and new office in the case of a director of companies, ministers of religion, departmental appointments, or where salaries were paid "free of tax," and in the case of appointments under railway companies.

The fact that the duties attached to an office were enlarged or diminished did not of itself involve assessment as for a new office, *e.g.*, where a director was appointed to the executive committee of directors, for which he received additional remuneration, such appointment did not constitute a new office (*May v. Falk* (1932), 17 T.C. 218). Every directorship, however, was a separate source and assessable as such.

If on a change of office a person would be assessable as on a new and discontinued basis, he could claim to have the preceding year basis continued, provided that he could show that (a) his average net emoluments from the new office for the first twelve months of his tenure thereof did not exceed by more than 20% his average monthly net emoluments from the old office for the last twelve months of his tenure thereof, and (b) the duties of the offices required the holder to devote substantially the whole of his time to the performance of his duties therein. (Where either office was held for less than twelve months, the average emoluments for the period of tenure of the office had to be taken instead of those for twelve months.) He was then entitled to require that all his emoluments arising from the new and old offices should be assessed as if they had arisen from one and the same office, *i.e.*, on the "previous year" basis. Notice had to be given to the Inspector of Taxes within 18 months after the end of the year of assessment in which he entered the new office (§ 26—1935).

Weekly manual wage earners were assessed on the actual income of each half-year to 5th October and 5th April, half allowances being given in the first half, the balance in the second.

## APPENDIX XVII.

## DOUBLE TAXATION

(FINANCE ACT, 1947, NINTH SCHEDULE).

## PART I.

PROVISIONS AS TO RELIEF FROM INCOME TAX AND THE PROFITS TAX BY WAY  
OF CREDIT IN RESPECT OF FOREIGN TAX.*Interpretation.*

1.—(1) In this Part of this Schedule, except where the context otherwise requires—

“the United Kingdom taxes” means income tax and the profits tax;

“foreign tax” means, in relation to any territory arrangements with the Government of which have effect by virtue of Part V of the Finance (No. 2) Act, 1945, any tax chargeable under the laws of that territory for which credit may be allowed under the arrangements;

“foreign income tax” means any foreign tax which corresponds to income tax;

“income,” in relation to the profits tax, means profits.

(2) Where arrangements having effect by virtue of Part V of the said Act provide for any tax chargeable under the laws of the territory concerned being treated as income tax or as a profits tax, that tax shall, notwithstanding anything in the preceding provisions of this paragraph, be treated as foreign income tax or foreign tax other than foreign income tax, as the case may be.

(3) Any reference in this Part of this Schedule to foreign tax or foreign income tax shall be construed, in relation to credit to be allowed under any arrangements, as a reference only to tax chargeable under the laws of the territory with the Government of which the arrangements were made.

*General.*

2.—(1) Subject to the provisions of this Part of this Schedule, where, under the arrangements, credit is to be allowed against any of the United Kingdom taxes chargeable in respect of any income, the amount of the United Kingdom taxes so chargeable shall be reduced by the amount of the credit.

(2) The credit to be allowed shall be first applied in reducing the amount of any profits tax chargeable in respect of the income and, so far as it cannot be so applied, in reducing the income tax chargeable in respect thereof.

(3) Nothing in this paragraph authorises the allowance of credit against any United Kingdom tax against which credit is not allowable under the arrangements.

*Requirement as to residence.*

3. Credit shall not be allowed against the profits tax for any chargeable accounting period or against income tax for any year of assessment unless the person in respect of whose income the tax is chargeable is resident in the United Kingdom for that period or year.

*Limit on total credit—the profits tax.*

4. The amount of the credit to be allowed against the profits tax in respect of any income for foreign tax shall not exceed the profits tax attributable to that income.

*Limit on total credit—income tax.*

5.—(1) The amount of the credit to be allowed against income tax in respect of any income for foreign tax shall not exceed the sum which would be produced by computing the amount of that income in accordance with the Income Tax Acts, and then charging it to income tax for the year of assessment for which the credit is to be allowed, but at the following rate, that is to say—

- (a) in the case of a person whose income is chargeable to income tax at the standard rate only, a rate ascertained by dividing the income tax payable by him for the year by the amount of his total income for the year;
- (b) in the case of a person part of whose total income is chargeable to income tax at a rate or rates in excess of the standard rate, the sum of the following rates—

- (i) the rate which would have been the appropriate rate in his case if his income had been chargeable at the standard rate only; and

- (ii) the rate ascertained by dividing the surtax payable by him for the year by the amount of his total income for the year:

Provided that where, under the arrangements, credit is not to be allowed against surtax for the year, the rate shall be calculated in all cases as in the case of persons whose incomes are chargeable to income tax at the standard rate only, and where, under the arrangements, credit is not to be allowed except against surtax for the year, the rate shall be that ascertained by dividing the surtax payable by the person in question for the year by the amount of his total income for the year.

(2) For the purpose of determining the said rate, the tax payable by any person for any year shall be computed without regard to any relief in respect of life assurance premiums and without any reduction thereof for any credit allowed or to be allowed under any arrangements having effect by virtue of Part V of the Finance (No. 2) Act, 1945, but shall be deemed to be reduced by any tax which, otherwise than under Rule 20 of the General Rules, he is entitled to charge against any other person, and the total income of any person shall be deemed to be reduced by the amount of any income the income tax upon which he is entitled to charge as aforesaid.

6. Without prejudice to the provisions of the last preceding paragraph, the total credit to be allowed to a person against income tax for any year of assessment for foreign tax under all arrangements having effect by virtue of Part V of the Finance (No. 2) Act, 1945, shall not exceed the total income tax payable by him for that year of assessment, less any tax which, otherwise than under Rule 20 of the General Rules, he is entitled to charge against any other person.

*Effect on computation of income of allowance of credit.*

7.—(1) Subject to the provisions of this paragraph, where credit for foreign tax falls to be allowed against any of the United Kingdom taxes in respect of any income, no deduction for foreign tax (whether in respect of that or any other income) shall be made in computing the amount of that income for the purposes of the profits tax.

(2) Where the income includes a dividend and, under the arrangements, foreign tax not chargeable directly or by deduction in respect of the dividend is to be taken into account in considering whether any, and if so what, credit is to be allowed against the United Kingdom taxes in respect of the dividend, the amount of the income shall, for the purposes of the profits tax, be treated as increased by the amount of the foreign tax not so chargeable which falls to be taken into account in computing the amount of the credit.

(3) Notwithstanding anything in the preceding provisions of this paragraph, where part of the foreign tax in respect of the income (including any foreign



tax which, under sub-paragraph (2) of this paragraph, falls to be treated as increasing the amount of the income) cannot be allowed as a credit against any of the United Kingdom taxes, the amount of the income shall be treated for the purposes of the profits tax as reduced by that part of that foreign tax.

8.—(1) Where credit for foreign tax falls to be allowed against any of the United Kingdom taxes in respect of any income, the following provisions of this paragraph shall have effect as respects the computation, for the purposes of income tax, of the amount of that income.

(2) Where the income tax payable depends on the amount received in the United Kingdom, the said amount shall be treated as increased by the amount of the credit allowable against income tax.

(3) Where the last preceding sub-paragraph does not apply—

- (a) no deduction shall be made for foreign tax (whether in respect of the same or any other income) ; and
- (b) where the income includes a dividend and under the arrangements foreign tax not chargeable directly or by deduction in respect of the dividend is to be taken into account in considering whether any, and if so what, credit is to be allowed against the United Kingdom taxes in respect of the dividend, the amount of the income shall be treated as increased by the amount of the foreign tax not so chargeable which falls to be taken into account in computing the amount of the credit ; but
- (c) notwithstanding anything in the preceding provisions of this sub-paragraph, where any part of the foreign tax in respect of the income (including any foreign tax which, under paragraph (b) of this sub-paragraph, falls to be treated as increasing the amount of the income) either falls to be allowed as a credit against the profits tax, or cannot be allowed as a credit against any of the United Kingdom taxes, the amount of the income shall be treated for the purposes of income tax as reduced by that part of that foreign tax.

(4) In relation to the computation of the total income of a person for the purpose of determining the rate mentioned in paragraph 5 of this Part of this Schedule, the preceding provisions of this paragraph shall have effect subject to the following modifications—

- (a) for the reference in sub-paragraph (2) to the amount of the credit allowable against income tax, there shall be substituted a reference to the amount of the foreign tax in respect of the income (in the case of a dividend, foreign tax not chargeable directly or by deduction in respect of the dividend being left out of account) ; and
- (b) paragraphs (b) and (c) of sub-paragraph (3) shall not apply,

and subject to those modifications shall have effect in relation to all income in the case of which credit falls to be allowed for foreign tax under any arrangements for the time being in force by virtue of Part V of the Finance (No. 2) Act, 1945.

*Special provisions as to dividends.*

9. Where, in the case of any dividend, foreign tax not chargeable directly or by deduction in respect of the dividend is, under the arrangements, to be taken into account in considering whether any, and if so what, credit is to be allowed against the United Kingdom taxes in respect of the dividend, the foreign tax not so chargeable which is to be taken into account shall be that borne by the body corporate paying the dividend upon the relevant profits in so far as it is properly attributable to the proportion of the relevant profits which is represented by the dividend.

The relevant profits are—

- (a) if the dividend is paid for a specified period, the profits of that period ;
- (b) if the dividend is not paid for a specified period, but is paid out of specified profits, those profits ;

- (c) if the dividend is paid neither for a specified period nor out of specified profits, the profits of the last period for which accounts of the body corporate were made up which ended before the dividend became payable :

Provided that if, in a case falling under sub-paragraph (a) or sub-paragraph (c) of this paragraph, the total dividend exceeds the profits available for distribution of the period mentioned in the said sub-paragraph (a) or the said sub-paragraph (c), as the case may be, the relevant profits shall be the profits of that period plus so much of the profits available for distribution of preceding periods (other than profits previously distributed or previously treated as relevant for the purposes of this paragraph or paragraph 9 of the Seventh Schedule to the Finance (No. 2) Act, 1945) as is equal to the excess ; and for the purposes of this proviso the profits of the most recent preceding period shall first be taken into account, then the profits of the next most recent preceding period, and so on.

10. Where—

- (a) the arrangements provide, in relation to dividends of some classes, but not in relation to dividends of other classes, that foreign tax not chargeable directly or by deduction in respect of dividends is to be taken into account in considering whether any, and if so what, credit is to be allowed against the United Kingdom taxes in respect of the dividends; and
- (b) a dividend is paid which is not of a class in relation to which the arrangements so provide.

then, if the dividend is paid to a company which controls, directly or indirectly, not less than one half of the voting power in the company paying the dividend, credit shall be allowed as if the dividend were a dividend of a class in relation to which the arrangements so provide.

11. Any relief granted under section thirty-one of the Finance Act, 1946 (which provides for relief from income tax on dividends from companies resident abroad) shall, for the purposes of paragraph 2 of this Part of this Schedule, be deemed to reduce the amount of United Kingdom income tax chargeable in respect of the dividend in question.

*Miscellaneous.*

12. Credit shall not be allowed under the arrangements against the United Kingdom taxes chargeable in respect of any income of any person if he elects that credit shall not be allowed in respect of that income.

13.—(1) Subject to the provisions of paragraph 15 of this Part of this Schedule, any claim for an allowance by way of credit for foreign tax in respect of any income shall be made to the surveyor not later than six years from the end of the relevant year of assessment, and, if the surveyor objects to any such claim, it shall be heard and determined by the Special Commissioners as if it were an appeal to them against an assessment under Schedule D, and the provisions of the Income Tax Acts relating to the statement of a case for the opinion of the High Court on a point of law shall, with the necessary modifications, apply accordingly.

(2) In this paragraph, the expression “the relevant year of assessment” means, in relation to credit for foreign tax in respect of any income, the year of assessment for which that income falls to be charged to income tax or would fall so to be charged if any income tax were chargeable in respect thereof.

14.—(1) The provisions of this paragraph shall have effect where, by virtue of a notice given under section twenty-two of the Finance Act, 1937 (which relates to subsidiary companies), profits of a body corporate fall to be treated for any of the purposes of the enactments relating to the profits tax as profits of another body corporate :

Provided that this paragraph shall not apply where credit is not allowable under the arrangements against the profits tax.

(2) Any election under paragraph 12 of this Part of this Schedule as respects any income of the first mentioned body corporate and any claim for an allowance by way of credit for foreign tax in respect of any income of the first mentioned body corporate must be made jointly by both bodies corporate.

(3) If both bodies corporate jointly so elect, any credit falling to be allowed for foreign income tax in respect of income of the first mentioned body corporate shall, notwithstanding anything in paragraph 2 of this Part of this Schedule, be applied first in reducing the income tax chargeable in respect of that income.

15. Where the amount of any credit given under the arrangements is rendered excessive or insufficient by reason of any adjustment of the amount of any tax payable either in the United Kingdom or under the laws of or of any other territory, nothing in the Income Tax Acts or in the enactments relating to the profits tax limiting the time for the making of assessments or claims for relief shall apply to any assessment or claim to which the adjustment gives rise, being an assessment or claim made not later than six years from the time when all such assessments, adjustments and other determinations have been made, whether in the United Kingdom or elsewhere, as are material in determining whether any and if so what credit falls to be given.

## PART II.

### APPLICATION OF PART I.

1. In the case of income which is chargeable neither to excess profit tax nor to the profits tax, the Seventh Schedule to the Finance (No. 2) Act, 1945, shall apply as respects income tax for the year 1946-47 or any previous year of assessment and Part I of this Schedule shall apply as respects income tax for the year 1947-48 or any subsequent year of assessment.

2. In the case of profits chargeable to excess profits tax or the profits tax, the said Seventh Schedule shall apply in relation to the allowance of credit—

- (a) against excess profits tax ;
- (b) against the profits tax for any chargeable accounting period ending at or before the end of the year nineteen hundred and forty-six ;
- (c) against so much of the profits tax for any chargeable accounting period ending after the end of the said year as is apportionable to any part of the period falling before the end of the said year ;
- (d) against any income tax chargeable in respect of profits for a period falling wholly before the end of the said year ; and
- (e) against so much of any income tax chargeable in respect of profits for a period falling partly before and partly after the end of the said year as is properly attributable to the profits for the part of the period which ends at the end of the said year,

and, save as aforesaid, Part I of this Schedule shall apply.

3. Where a period on the profits of which foreign tax is chargeable falls partly before and partly after the end of the said year, and the profits in question are chargeable to excess profits tax or the profits tax, all such apportionments shall be made of that foreign tax between the two parts of the period as are necessary to secure that credit is allowed for the proper proportions thereof under the said Seventh Schedule and under Part I of this Schedule respectively.

4.—(1) In this Part of this Schedule, the expression " foreign tax " has the same meaning as in Part I of this Schedule, and references to profits chargeable to excess profits tax or profits chargeable to the profits tax shall be construed as references to profits which fall to be included in computing the profits of a trade or business for any chargeable accounting period for the purposes of those taxes respectively.

(2) Any apportionment of profits tax which falls to be made under subparagraph (c) of paragraph 2 of this Part of this Schedule shall be made in the same manner as for the purposes of section nineteen of the Finance (No. 2) Act, 1939.

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